

Bond University

DOCTORAL THESIS

The evolution of the regulation governing superannuation funds since 1936

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**THE EVOLUTION
OF THE
REGULATION
GOVERNING SUPERANNUATION FUNDS
SINCE 1936**

by

Josephine Cleary

A thesis submitted to the Bond University Faculty of Law
in fulfilment of the requirements for
the Degree of
Doctor of Philosophy.

October 2010

Gold Coast
Australia

CERTIFICATE

This thesis is submitted to Bond University in fulfilment of the requirements for the Degree of Doctor of Philosophy.

This thesis represents my own work and contains no material which has been previously submitted for a degree or diploma at this University or any other institution.

Signature: _____

Date: 25 October 2010

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Josephine Cleary

Gold Coast October 2010

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ABSTRACT

By Federation, the community's attitude towards the aged poor was changing. Politicians accepted that support for the aged was a collective responsibility for the whole community. The aged pension was introduced. A function of the Federal Government is to raise sufficient revenue from the private sector to cover expenditure with an equitable and efficient allocation of the tax burden. Payment of the pensions to the aged forms part of the Federal Government's expenditure.

The basis for the Federal Government's retirement policy arose because the analysis of the demographics and economic projections indicated that the social security system could not support retirees indefinitely. The Federal Government had to take a proactive role in planning and developing strategies for providing retirement income for the population.

This thesis analyses the evolution of the regulation of the legislation framework from 1936. It involves reviewing the effectiveness of providing tax incentives to encourage people to save. It analyses the evolution of the regulation of superannuation funds needed to protect members' benefits, make trustees accountable for their responsibilities and minimise, if not prevent abuse of the superannuation system. The evolution can be seen to be three phases, all connected with circumstances that required the Federal Government's attention. Firstly, there were the measures to encourage people to save for their retirement. Secondly, there was the protection of members' benefits. This occurred with the introduction of the *Occupational Superannuation Standards Act* ('OSSA') that replaced the regulation by the *Income Tax Assessment Act*. Thirdly, there was making trustees accountable for their responsibilities. This occurred with the introduction of the *Superannuation Industry (Supervisions) Act 1993* ('SISA'), which replaced the OSSA.

ABSTRACT

The thesis shows that the evolved legislation framework allows the Regulators to control the quality and competency of trustees, the disclosure of information making members fully informed about their retirement savings and impose penalties and make the trustees accountable for their responsibilities.

It proves the hypothesis. The legislation regulating superannuation funds has evolved to encourage people to save for their own retirement in line with the Federal Government's policy. It makes trustees of superannuation funds accountable for their responsibilities so that members' benefits will be available when required. By the introduction of a penalty regime, it minimises abuse of the superannuation system.

Gold Coast, October 2010

Josephine Cleary
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LEGISLATION

Acts Interpretation Act 1901
Administrative Appeals Tribunal Act 1975
Administrative Decisions (Judicial Review) Act
Australian Bankruptcy Act 1966
Australian Prudential Authority Act 1998
Banking Act 1959
Companies (Applications of Laws) Act 1981
Conciliation and Arbitration Act 1904
Commonwealth of Australia Constitution Act 1900
Companies Code Act 1981
Companies (Application of Laws) Act 1981
Companies and Securities (Interpretation and Miscellaneous Provisions) (Application of Laws) Act 1981
Corporations Act 1989
Corporations Act 2001
Crimes Act 1914
Criminal Code Act 1995
Crimes (Taxation Offences) Act 1980
Financial Corporations Act 1974
Financial Sector (Collection of Data) Act 2001
Income Tax Assessment Act 1915
Income Tax Assessment Act 1936
Income Tax Assessment Act 1997
Income Tax Act 1936
Income Tax (Companies and Superannuation Funds) Act 1976
Income Tax Rates Act 1986
Invalid and Old Age Pensions Act 1908
Life Insurance Act 1945
Occupational Superannuation Standards Act 1987
Superannuation Contributions Tax (Assessment and Collection) Act 1997
Superannuation Guarantee (Administration) Act 1992
Superannuation Industry (Supervision) Act 1993
Surcharge Contributions Tax Imposition Act 1997

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Case W100 89 ATC 813
Case W109 89 ATC 859
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Case Y55 91 ATC 474
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Case QT85/1074 and Commissioner of Taxation

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LIST OF ABBREVIATIONS

AAT	Administrative Appeals Tribunal
AATA	<i>Administrative Appeals Tribunal Act 1975</i>
ASFA	Association of Superannuation Funds of Australia
APRA	Australian Prudential Regulation Authority
APRC	Australian Prudential Regulation Commission
ASIC	Australian Security and Investments Commission
ATO	Australian Taxation Office
CA	<i>Corporations Act 2001</i>
ITAA	<i>Income Tax Assessment Act 1936</i>
ITAA 97	<i>Income Tax Assessment Act 1997</i>
ISC	Insurance and Superannuation Commission
SISA	<i>Superannuation Industry (Supervision) Act 1993</i>
SISR 1994	Superannuation Industry (Supervision) Regulations 1994
OSSA	<i>Occupational Superannuation Standards Act 1987</i>
OSSR	<i>Occupational Superannuation Standards Regulations</i>
TAA	<i>Taxation Administration Act 1953</i>
RSE	Registrable superannuation entities
SSC	Senate Select Committee
SGAA	<i>Superannuation Guarantee (Administration) Act 1992</i>
SRCA	<i>Superannuation (Resolution of Complaints) Act 1993</i>
SWG	Superannuation Working Group
TA	Taxpayer Alerts

CHAPTER 1

INTRODUCTION

Working to live is a principle of life. Providing for life after a working life is an established principle of society. Who is responsible for providing funds for the life after a working life and how this is to be achieved are questions that have been addressed for many years. Superannuation funds provide a mechanism to fund retirement. This thesis analyses the evolution of their regulation in Australia.

Chapter 1 first provides a background to the thesis. It then describes the hypothesis and methodology. Thirdly, it provides the structure of the thesis in proving the hypothesis. Finally, it details the limitations of the thesis.

1.1 Background

This background provides the context for the hypothesis. It sets out the broad history of superannuation and the government response. The hypothesis flows directly from this context.

In the nineteenth century, relatives and friends were expected to provide care for the old. Where this care was not available, welfare for the aged was provided by charitable organisations. Support was intended to alleviate only the worst poverty and not create ‘a class that would become permanently dependent on the State’.¹

On 30 November 1839, George Griffiths, Inspector in the Colonies of the Bank of Australasia, now Australia and New Zealand Banking Group Ltd, proposed what is likely to have been the first pension fund established in Australia.² It was not until 5 October

¹ T H Kewley, *Social Security in Australia, 1900-72*, (Sydney University Press, 1973) 15, quoting Renwick giving evidence to the Royal Commission on Public Charities in 1898.

² Damien Cash, a former historian on the staff of ANZ Group Archive, *History – Our Company*, October 1989, ANZ <<http://www.anzbank.com.au>>.

1841 that the bank's directors in London seriously considered the establishment of an 'Officers' Retiring Fund'. The concept was approved in principle and actuarial advice sought. On 21 April 1842, the directors considered the plans and resolved to establish the fund. The directors declared that the aim of the fund was to provide for those officers 'who from age and length of meritorious service, or from physical or mental inability induced while in the service, should on their retirement appear to be entitled to a participation in the benefits thereof'.³

Shortly after in 1862, the Bank of New South Wales⁴, now Westpac Banking Corporation, established the second superannuation fund⁵.

By Federation, a more sympathetic attitude by the community towards the aged poor was gaining acceptance. The politicians accepted that support for the aged was not solely the responsibility of the family shared if necessary with public charities, but a collective responsibility for the whole community.⁶ The *Commonwealth of Australia Constitution Act 1900* ('Constitution') recognised the possibility of the Federal Government providing for

The Bank of Australasia was established under Royal charter in London in 1835. In 1837, the Union Bank of Australia, an Anglo-Australian bank, was established. In 1852, the English, Scottish and Australian Bank, also an Anglo-Australian Bank, was established. In 1951, the Bank of Australia merged with the Union Bank of Australia to form the ANZ Bank.

In 1970, the ANZ Bank merged with the English, Scottish and Australian Bank Limited to form the present organisation, Australia and New Zealand Banking Group Limited.

³ Ibid 1.

⁴ The Westpac Group *Westpac - Our History*, <<http://www.Westpac.com.au>>. The company was established in 1816 under a charter of incorporation provided by governor Lachlan Macquarie, commenced business in 1817 and was subsequently incorporated under the *Bank of New South Wales Act 1850* of the New South Wales Parliament. In 1982, it merged with The Commercial Bank of Australia Ltd to form the Westpac Banking Corporation.

⁵ The Fund established was a Fidelity, Guaranteed and Provident Fund.

⁶ J Dixon, *Australia's Policy Towards the Aged: 1890-1972* (Canberra College of Advanced Education, 1977) 4-5.

Ibid. Some States provided a pension prior to the introduction of the Commonwealth 18-22.

the aged by giving it the power to legislate for pensions for them.⁷

*The Invalid and Old Age Pensions Act 1908*⁸ set out the

requirements for persons to be eligible for the age pension.

Eligibility was according to character, race, age, residency and means.⁹

Initially, the Federal Government's policy was to encourage employers to contribute towards employees' retirement. The encouragement took the form of tax incentives. These tax incentives were deductions for contributions by the employers, exemption from income tax for the income of the fund that invested the contributions and tax concessions for part of the benefits received by the employees on retirement.

In 1915, the first income tax assessment act, *Income Tax Assessment Act 1915* ('ITAA 1915'), recognised retirement when deductions were allowed in respect of 'sums set aside or paid by an employer of labour ... to provide individual personal benefits, pensions, or retiring allowances to employees'¹⁰, income of superannuation funds was exempt¹¹ and retirement allowances and gratuities paid in a lump sum to any person were excluded from income¹².

⁷ *Commonwealth of Australia Constitution Act 1900* ('Constitution') s 51(xxiii).

⁸ *Invalid and Old Age Pensions Act 1908*, No 17 1908.

⁹ *Invalid and Old Age Pensions Act 1908* s 16.

The character and race provisions of the *Invalid and Old Age Pensions Act 1908* denied the age pension to people who were not of 'good character' as well as Aliens (ie non-residents), non-Australian born Asians, Australian aborigines, Africans, Pacific Islanders and New Zealand Maoris. These provisions were progressively removed over the next 60 years.

¹⁰ *Income Tax Assessment Act 1915* (Cth) s 18(1)(j). An employer was allowed a deduction for money contributed to a fund established to provide 'benefits, pensions or retiring allowances' for employees, provided the Commissioner was satisfied that the rights of the employees were fully secured.

¹¹ *Ibid* s 11(f).

¹² *Ibid* s 14(g). Retiring allowances and gratuities paid as a lump sum were excluded from an individual's income. Superannuation benefits paid as a pension were included in the recipient's taxable income.

ITAA 1915 provided an exemption from income tax for income of ‘a provident, benefit, or superannuation fund established for the benefit of the employees in any business’.¹³ This exemption¹⁴ continued to apply when the *Income Tax Assessment Act 1936* (*ITAA*) was introduced.¹⁵

1.2 Demographic and projected economic analysis¹⁶

This analysis is restricted to data relating to the ageing population, retirement and the work force available to support retirees. For the purposes of this analysis, a retiree is defined as a person aged 65 years or more.

As is demonstrated in Table 1, based on statistics both past and projected, Australia's population has grown during the 20th century and continues to grow in the 21st century.¹⁷

¹³ See above n 11.

¹⁴ *ITAA* s 23(j)(i).
Amounts paid as a pension continued to be included in the recipient's taxable income. Five percent of the capital amount of any allowance, gratuity or compensation where paid in a lump sum in consequence of retirement from or the termination from employment was included in a person's taxable income – *ITAA* s 26(d).
A tax deduction was allowed for contributions made by an employer to a fund established to provide individual personal benefits, pensions or retiring allowances for employees provided the employer was under a legal obligation to set apart or pay the sum and the rights of the employees were fully secured – *ITAA* s 66.

¹⁵ *Income Tax Assessment Act 1936*, No 27 1936.

¹⁶ Except where noted otherwise, all statistical data have been sourced from publications prepared and published by the Australian Bureau of Statistics ('ABS').

¹⁷ ABS, *1901-2005: Australian Historical Population Statistics, Population by Age and Sex 2006*, 3105.0.65.001 (24 July 2007) Table 19; 2007: *Year Book Australia, 2009-10*, 1301.0 (4 June 2010) [7.11].

Projections: ABS 2006 to 2101, 78.

Assumptions 9-10:

1. the base population is the preliminary estimated resident population at 30 June 2007;
2. total fertility rates 2.0 babies per woman by 2021 and then remain constant;
3. life expectancy at birth will reach 93.0 years for males and 96.1 years for females by 2056 and remain constant thereafter. Male and female life expectancy at birth will continue to increase by 0.30 years and 0.25 years per year respectively until 2056;
4. net overseas migrations are included in projections at 220,000 people per year from 2011.

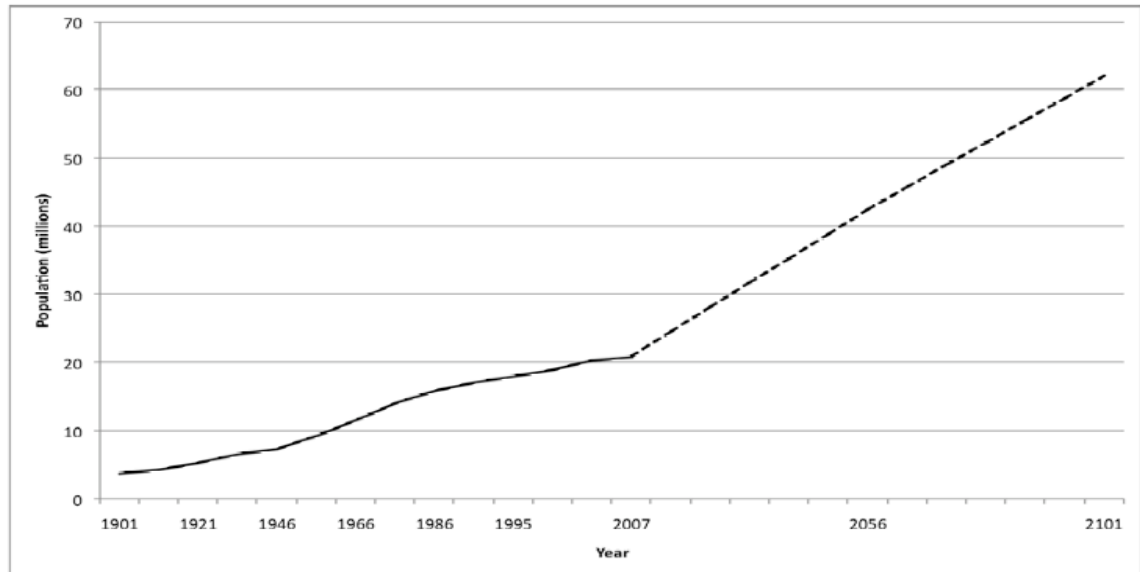


Table 1: Australian population projected to 2101

In addition to Australia's population growing, it is ageing through sustained low levels of fertility resulting in proportionally fewer children in the population, and increasing life expectancy. In a Media Release on 17 December 2004, the Australian Bureau of Statistics ('ABS') announced that:

between June 1984 and June 2004, the proportion of the population aged 15-64 years remained relatively stable, increasing from 66% to 67% of the total population. The proportion of people aged 65 years and over increased from 10% to 13%. During the same period, the proportion of the population aged 85 years and over increased by 163%. The proportion aged under 15 years decreased from 24% to 20%.¹⁸

Improvements in living conditions in the early-20th century, such as better water supply, sewerage systems, food quality and health education resulted in an overall decline in mortality.¹⁹ The projected continued increase in ageing population reflected the increase in births after World War II, the 'baby boom generation'.²⁰

¹⁸ ABS, 'Population by Age and Sex, Australian States and Territories June 2004', (Media Release, 3201.0, 17 December 2004).

¹⁹ ABS, *Australian Social Trends*, 1995, 4102.0, 20 June 1995, quoting SK Jain, 'Trends in Mortality' (1994) National Centre for Epidemiology and Population Health.

²⁰ ABS, *Australian Social Trend*, 1996, 4102.0, 24 June 1996.

The continuing reduction in mortality in the latter half of last century was attributed to improving social conditions and advances in medical technology such as mass immunisation and antibiotics.²¹ Increases in life expectancy were due in part to lower infant mortality, fewer deaths among young adults from motor vehicle accidents and fewer deaths among older men from heart disease.²² The reduction in the number of deaths from heart disease has been related to medical advances and behavioral changes such as improvements in diet and a reduction in smoking.²³

Since the turn of the 20th century, the percentage of population aged 65 years or over compared with the total population increased.²⁴ Table 2 demonstrates this percentage increase of population and the continuation of this trend in future years.

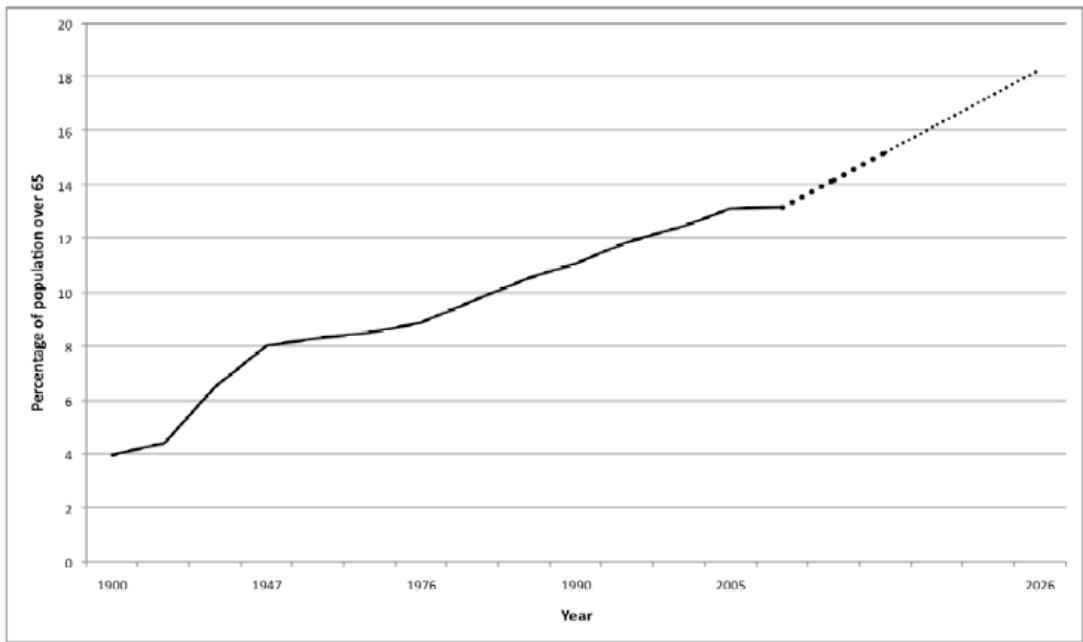


Table 2: Percentage of total population 65 years of age and over

21 See above n 19.
22 Ibid.
23 Ibid.
24 ABS, *Australian Historical Population Statistics 2008*, 3105.0.65.001, 5 August 2008
ABS, *Population Projections, Australia, 2006 to 2101*, 3222.0 44.

The median age is also an indicator of an ageing population, the median age being the age at which half the population is older and half is younger.²⁵

Table 3 shows the increase in the median age of the Australian population with a decrease in the years following World War II. This Table demonstrates a continuation of this trend in future years.

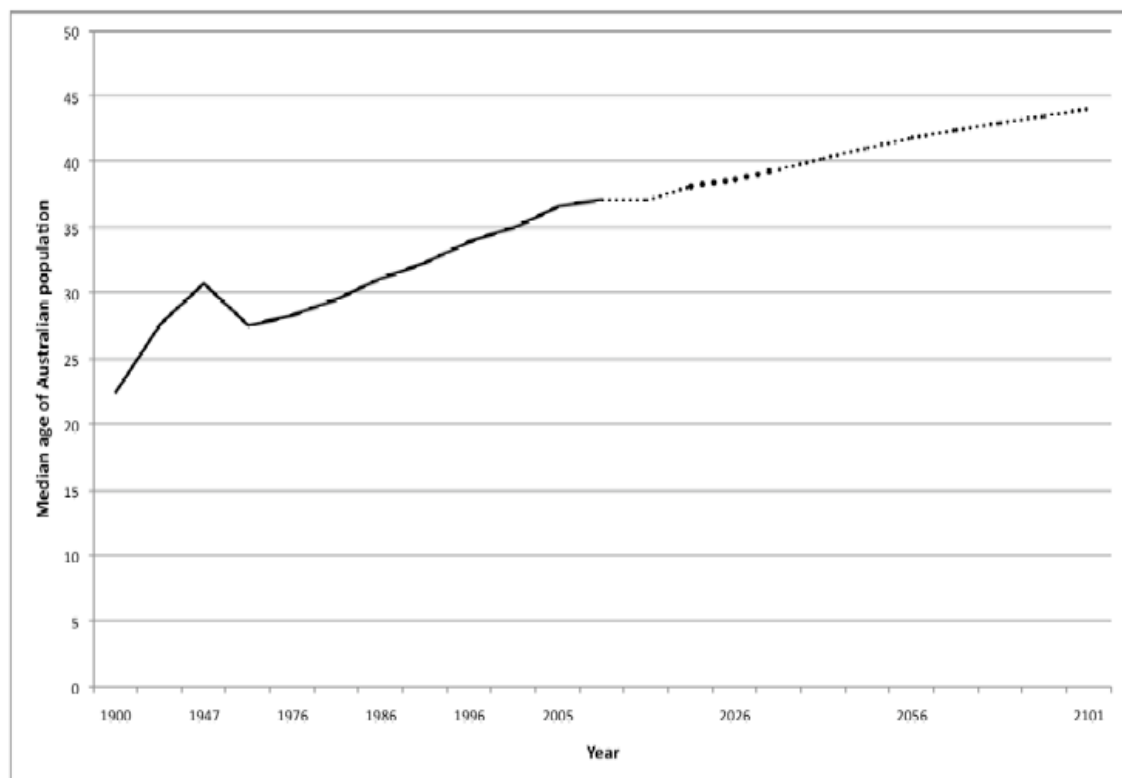


Table 3: Median age of Australian population in years

Demographic and projected economic analysis established that the social security system could not continue to support retirees indefinitely. In addition to a continuing increase in the numbers of the aging population, there was an increase in the number of retirees dependent on the aged pension.

²⁵ ABS, *2006 Year Book Australia*, 1301.0 Table 5.16 114.
 ABS, *Estimated Resident Population by Sex and Age States and Territories of Australia*, 3201.0 Table 5, 24.
 ABS, *Population Projections, Australia, 2006 to 2101*, 80.

Table 4 shows that the percentage of the population depending on the pension increased consistently except during the decade from 1976 to 1986 where there was only a slight increase.

Year	Persons receiving the pension	Percentage of population
1947/48	302,854	3.93%
1956	446,207	4.73%
1966/1967	651,363	5.52%
1976	1,158,657	8.26%
1986	1,324,600	8.27%
2000	1,730,000	9.03%
2005	1,915,000	9.42%

Table 4: Persons receiving the pension

As is shown in Table 5, there was also an increase in the dependency ratios. The dependency is the ratio of people aged 65 years and over per 100 population of the working age (those aged 15-64 years).

	1971²⁶	1984²⁷	2003²⁸	2007²⁹	2051³⁰
Aged 65+	13.2	15.3	19	20	33

Table 5: Dependency ratios

A higher proportion of persons participating in higher education also contributed to the relative decrease in the number employed.³¹ There was a trend for increased attendance at tertiary institutions. In 1984, accurate figures were collected for the first time to record

²⁶ ABS, 1986 Census Chapter 6.

²⁷ Ibid.

²⁸ Occupational Health and Safety Department, *Surveillance Alert OHS and the Ageing Workforce* May 2005.

²⁹ ABS, *Australian Social Trends Future Population Growth and Ageing*, 4102.0 2009, 23 March 2009.

³⁰ Ibid.

³¹ Australian Government, Department of Education, Employment and Workplace Relations, *Students 1994: Selected Higher Education Student Statistics*, February 1995, 15.

this trend. Between the years 1984 to 1994, the total number of students enrolled for tertiary education increased from 357,373 to 585,396 - an increase of 63.81%. Percentage increase of total population was 14.61%.³²

By the year 2000, the total number of students enrolled for tertiary education reached 695,485³³ with a further increase to 957,176 by 2005.³⁴ This number represented 4.69% of the total population.

The social security system would have an increased burden if there were a significant trend to earlier retirement and changes in attitude about the level of retirement income considered satisfactory³⁵. In the 2009 Budget, the Federal Government announced that the age pension age would be gradually increased to 67 years of age.³⁶ The new pension changes will apply to new pension entrants from 1 July 2017 which will mean that it applies to people who are 57 years of age or younger on 1 July 2009.

Demographic and projected economic analysis since the beginning of the 20th century confirmed the need for affirmative action in providing funding for life after work.

1.3 Government's reaction and strategy

To reduce the numbers relying on the old age pension and therefore the burden on public funds, the Federal Government's policy for funding the retirement of the Australian population has

³² Ibid. Population in 1984: 15,579,391; population in 1994: 17,854,738.

³³ Australian Government, Department of Education, Employment and Workplace Relations, *Students 2000: Selected Higher Education Student Statistics*, February 2002, 6.

³⁴ Australian Government, Department of Education, Employment and Workplace Relations, *Students 2005: Selected Higher Education Student Statistics*, September 2006, 6.

³⁵ The Treasurer, the Hon John Dawkins MP, *Security in Retirement, Planning for Tomorrow Today* (1992), 2.
Whereas the objective of government in relation to age pension has been to ensure a minimum level of income, currently 25% of average weekly earnings, superannuation tends to target post retirement earnings to some percentage of pre-retirement earnings.

³⁶ The Treasurer, the Hon Wayne Swan MP, *2009 Federal Budget*, 14 May 2009.

been and remains for individuals, where possible, to provide for their own retirement by their savings, or those of their employers, through contributions to superannuation funds. It recognised contributing to a superannuation fund was one method to save for retirement. The Federal Government investigated and adopted methods for encouraging savings to increase the amount of funds available for retirement income.

1.3.1 Voluntary contributions

To encourage participation in superannuation funds, the Federal Government provided incentives in the form of tax concessions for voluntary contributions. Subject to compliance with provisions of the *ITAA* initially and subsequently the *Income Tax Assessment Act 1997* ('*ITAA 97*'), these incentives allowed for tax concessions:

- deductions and rebates for contributions to superannuation funds – employer contributions and personal contributions;
- concessional tax treatment of benefits paid from superannuation funds to employees on retirement; and
- concessional tax treatment of income derived by superannuation funds.

Before 1952, income of non-employee superannuation funds was not exempt from income tax. For reasons of equity and to encourage self-employed persons to establish pension funds for their benefit,³⁷ the Federal Government extended the application of these tax incentives to the superannuation funds established for the contributions of 'eligible persons'.³⁸ A deduction for contributions made by self employed or employees who did not participate in superannuation benefits funded by an employer was

³⁷ The Treasurer, Sir Arthur Fadden, 'Income Tax and Social Services Contribution Assessment Bill (No 3) 1952' (Second Reading Speech delivered at the House of Representatives, Canberra, 18 September 1952).

³⁸ *ITAA* s 23(ja), as inserted *Income Tax and Social Services Contribution Assessment Act 1952*, No 90 1952. Date of Assent 18 November 1952, commencement 18 November 1952.

not allowed until 1980.³⁹ When this did occur, it was considered to be a significant incentive to encourage people who did not have the support of an independently funded superannuation scheme to make better provision for their retirement.⁴⁰

Other funds were developed by the Federal Government to cater for the various circumstances that arose to ensure that tax incentives were available for all who wished to save for their retirement.

1.3.2 *National Superannuation Scheme*

To implement its policy for funding retirement, the Federal Government explored different strategies to supplement the tax incentives provided for voluntary savings. In the 1970s, when reviewing its retirement income policy, the Federal Government considered the possibility of introducing a national superannuation scheme to implement its retirement income policy.⁴¹ One of the Terms of Reference of the Hancock Committee⁴² was ‘to make recommendations on a suitable national superannuation scheme’.⁴³ The Committee focused on the income in old age and retirement. This focus was with the concurrence of the Minister for Social Security.⁴⁴ Two main sources of funds were recognised as available to retired persons. These sources were pensions provided

³⁹ ITAA ss 82AAS, 82AAT, as inserted by *Income Tax Assessment Bill (No 4) 1980*.

⁴⁰ The Treasurer, the Hon John Howard ‘Income Tax Assessment Bill (No 4) 1980’ (Second Reading Speech delivered at the House of Representatives, Canberra, August 1980).

⁴¹ Treasury of Australia, ‘Towards higher retirement incomes for Australians: a history of the Australian retirement income System since Federation’ (Centenary Edition 2001) *Economic Round-up* 65-92, 75.

Proposals to introduce a universal contribution national superannuation or insurance scheme in Australia failed in 1928 and 1938.

⁴² Commonwealth of Australia, *Final Report of the National Superannuation Committee of Inquiry Part One*, Parl Paper No 155 (1976).

⁴³ Ibid.

T H Kewley *Social Security in Australia 1900-72* (Sydney University Press, 1973) 426-434. A proposal for a national superannuation scheme was submitted by R C Gates (ed), ‘Social Services in Australia’ (Economic Papers No 18 February 1965), 55-58. Later proposal was by R I Downing, ‘National Superannuation Means Test and Contribution’ (December 1968) Vol 44 No 108 *Economic Record*. Much bi-partisan discussion on the introduction of a national superannuation scheme preceded and followed these proposals.

⁴⁴ Ibid vii.

for the community through the age pensions scheme and the network of occupational superannuation schemes that provided pensions or lump sum benefits to some retired employees. Limited retirement benefit schemes were constructed for self-employed persons. Two schemes were considered appropriate choices for deliberation. The first was a flat rate, non-contributory scheme that freed the existing age pension from the means test but embodied modification in detail. A second scheme was considered more ambitious in respect of the benefits provided and would require levying of contributions related to personal income.⁴⁵ After deliberating on the two schemes, the Committee recommended a specific income related contributory scheme.

The proposed National Superannuation Scheme was to provide national superannuation pensions⁴⁶, ancillary benefits⁴⁷ and death benefits⁴⁸. Contributions to the National Superannuation Scheme were to be levied on incomes of persons and were to be assessed for each financial year. In effect, this would have been an additional tax on personal income. The levy proposed involved a 5 per cent surcharge on that part of income above 30 per cent of average weekly earnings.

⁴⁵ See above n 42.

⁴⁶ The universal pension was to be paid to all persons aged 65 or more if they satisfied the residence requirements. It was to be equal to about 25 per cent of the average weekly earnings per employed male unit, adjusted quarterly by reference to movements of a Pension Adjustment Index designed to ensure that the long term benefits rose proportionally to average weekly earnings. Payments were to be to women aged between 60-64 with phasing out by progressively raising the age of entitlement. These payments were subject to means test.

⁴⁷ Ancillary benefits included dependent spouse's allowance, dependent child's allowance, guardian's allowance and living alone allowance. Initially the ancillary benefits were to be subject to means test but reviewed in certain circumstances.

⁴⁸ Death benefits were to be paid upon the deaths of persons aged 19 years or more. The amounts paid were to be related to age at death and were to include both amounts unrelated to past contributions and additional contributory benefits.

The Federal Government decided not to adopt the scheme recommended by the majority of the Committee.⁴⁹ The Treasurer said that such a surcharge would have imposed a very heavy burden on middle and lower income workers.⁵⁰ Further, the scheme would also involve a major compulsory transfer of resources to the aged, including the aged on higher incomes, away from those in the workforce in need of assistance, including other dependent sections of the community such as invalids, single parents, the sick and unemployed.⁵¹ The Treasurer said that the freedom of choice individuals enjoyed in arranging their own affairs in respect of income in retirement should be retained.

In 1988, in its report to the Federal Government, the Social Security Review concluded on the introduction of a national superannuation scheme:

The opportunity for introducing such a scheme in Australia has now passed. Occupational superannuation is more firmly entrenched than ever, and the ageing of the population means that any unfunded scheme introduced now would probably face a financial crisis as the ratio of contributors to beneficiaries declined and benefit structures matured.⁵²

1.3.3 Compulsory Superannuation Contributions

In 1979, as a result of a Preliminary Report⁵³ to the Federal Government⁵⁴ by the Commonwealth Task Force on Occupational Superannuation Funds⁵⁵, the Treasurer and the Minister for

⁴⁹ The Treasurer, the Hon John Howard MP, 'Superannuation' (Press Release, No 68, 12 July 1979).

⁵⁰ Ibid.

⁵¹ Ibid.

⁵² Social Security Review *Towards a National Retirement Incomes Policy* (Issues Paper No 6 Commonwealth of Australia, 1988) 182.

⁵³ Commonwealth Taskforce, *Occupational Superannuation* (Preliminary Report, Commonwealth Government of Australia, August 1979).

⁵⁴ The Liberal-Country Party coalition government under Prime Minister the Rt Hon John Malcolm Fraser AC CH.

⁵⁵ Commonwealth Taskforce, *Occupational Superannuation* (Parliamentary Paper No 27, Parliamentary Library, Commonwealth Government of Australia, 1983), 4 [1.7].

Industrial Relations issued a joint press statement⁵⁶ indicating that it was concerned to ensure that union activities in relation to superannuation were not to circumvent wage indexation⁵⁷ guidelines but were directed towards meeting the genuine retirement needs of members and were subject to the same rules and standards as those applying to others involved in superannuation.

In 1983, the Hawke Labor Government supported the principles of employee superannuation. It initiated discussions with the Australian Council of Trade Unions ('ACTU') on the possibility of broadening access to superannuation throughout the workforce as part of the Government's negotiated Accord⁵⁸ with the trade unions.⁵⁹ 39% of the total workforce, with 25% of women and 'blue collar' workers, had superannuation.⁶⁰ Total Australian superannuation assets totalled approximately \$50 billion.⁶¹

56 The Hon John Howard MP and the Hon Tony Street MP, 'Occupational Superannuation' (Press Release, No 90, 6 September 1979).

57 Edna Carew, *The Language of Money* Australian and New Zealand Banking Group (1996).
The adjustment of wages to compensate for inflation. ... Wage indexation has existed for decades under different names such as 'cost-of-living adjustments'. It was introduced formally in Australia in 1975, reduced to partial indexation in 1976 and put to rest in 1981. It was revived in 1983 as the basis of the Labor government's Prices and Incomes Accord. The extent of indexation was reduced during the 1980s so that by the early 1990s the setting of pay rates by enterprise bargaining had become the centrepiece of the Accord.

58 Ibid.
An agreement on economic policy first made between the Australian Labor Party and the Australian Council of Trade Unions in February 1983, setting out policies on prices and incomes. The Accord provided for continual consultation between the government and the trade union movement and laid the basis for the establishment of the Economic Planning Advisory Council.

59 The Treasurer, the Hon P. Keating MP, 'Economy', Ministerial Statement, 19 May 1983.

60 Treasury of Australia, 'Towards higher retirement incomes for Australians: a history of the Australian retirement income System since Federation' (Centenary Edition 2001) *Economic Round-up*.

61 APRA Insight Issue Two 2007, Special Edition, Short History, Industry Super Funds.

In 1984, the ACTU launched campaigns for universal, fully vested superannuation. In 1987, the Arbitration Commission included in awards agreements of up to 3% contribution.⁶²

In the late 1980s, the Labor Federal Government developed a retirement incomes policy in recognition that the aging of the ‘baby boomer’ generation would compromise the ability of future governments to fund the age pension.

Voluntary superannuation was encouraged by continuing tax incentives, while reliance on the aged pension as the main provider of retirement incomes was to be minimised.⁶³ The introduction of compulsory employment based superannuation required employers to provide minimum levels of superannuation support for most of their employees.⁶⁴ This compulsory superannuation contribution was known as Superannuation Guarantee (‘SG’). The contribution rate progressively increased between 1992 to 2002 from 3% to 9% of salary⁶⁵. The Federal Government stated that SG would provide:

- a major extension of superannuation coverage to employees not currently covered by superannuation;
- an efficient method of encouraging employers to comply with their obligation to make contributions on behalf of their employees; and
- an orderly mechanism by which the level of employer superannuation support could be increased over time, consistent

⁶² In 1986, the Confederation of Australian Industry challenged the Commission’s decision in the High Court on the grounds that the Commissioner did not have the jurisdiction to rule on any claim relating to the payment of superannuation benefits as part of an industrial award as superannuation was not an industrial matter within the meaning of *Constitution* s 51(xxxv).

Constitution s 51(xxxv) limits the Commonwealth’s jurisdiction to conciliation and arbitration for the prevention and settlement of industrial disputes extending beyond the limits of any one state. The High Court validated superannuation as an ‘industrial matter’ under the *Conciliation and Arbitration Act – Re Manufacturing Grocers’ Employees Federation of Australia; Ex Parte Australian Chamber of Manufacturers* (1986) 160 CLR 341 357.

⁶³ The Treasurer, the Hon P J Keating MP, ‘Reform of the Taxation of Superannuation’ 25 May 1988.

⁶⁴ *Superannuation Guarantee (Administration) Act 1992* (‘SGAA’), No 111 1992, Date of Assent 21 August 1992, commencement 1 July 1992.

⁶⁵ SGAA s 11(1) (definition of ‘salary or wages’).

with the Government's retirement income policy objectives and the economy's capacity to pay.⁶⁶

In this way, in conjunction with the age pension, the Superannuation Guarantee would help to meet the challenges of Australia's aging population, the significant trend towards earlier retirement and changing community views about what level of retirement income is adequate.⁶⁷ A levy was required to be paid where employers failed to contribute a percentage of employee's earnings to a fully vesting superannuation fund.⁶⁸

A review of the results of this policy indicates success in relation to providing superannuation benefits for most employees. Table 6 shows the increase in the proportion of employees with superannuation coverage.

Date	Proportion of employees (e) with superannuation coverage
	%
February 1974 (a)	32
November 1988 (b)	55 (f)
November 1991 (b)	78 (f)
November 1993 (b)	89 (f)
November 1995 (b)	89 (f)
April to June 2000 (c)	91 (g)
April to July 2007 (d)	94

Table 6: Superannuation coverage in Australia⁶⁹

⁶⁶ The Hon John Dawkins MP above n 35, 24.
Senate Select Committee, Parliament of the Commonwealth of Australia, *Super Guarantee Bills* (1992) reviewed the introduction of *Superannuation Guarantee (Administration) Bill 1992* and associated Bills.

⁶⁷ Ibid 1-2.

⁶⁸ SGAA pt 3.

⁶⁹ ABS, *Australian Social Trends March 2009: Survey of Superannuation, February 1974; Superannuation, Australia, November 1988; Superannuation, Australia, November 1991; Superannuation, Australia, November 1993; Superannuation, Australia 1995; Superannuation Coverage and Financial Characteristics, Australia, April to June 2000; Employment Arrangements, Retirement and Superannuation, Australia, April to July 2007 (Reissue).*

- (a) Survey scope was civilians aged 15 years and over (except those who were inmates of goal, reformatories, etc).
- (b) Survey scope was people aged 15-74 years who had left school (except those in institutions).
- (c) Survey scope was people aged 15-69 years living in private dwellings.
- (d) Survey scope was people aged 15 years and over living in private dwellings.
- (e) Excluded those who were an owner manager of an incorporated enterprise in their main job.
- (f) Only people with a superannuation account attracting contributions were defined as having superannuation coverage.
- (g) Lump sums received more than one year ago but less than four years ago were excluded from the definition of 'superannuation coverage'.

The introduction of the SG in 1992 required reform of the prudential rules governing superannuation funds and a tightening of the preservation rules concerning access to superannuation benefits.⁷⁰

Table 7 shows the increase of the total amount of assets in all superannuation funds.

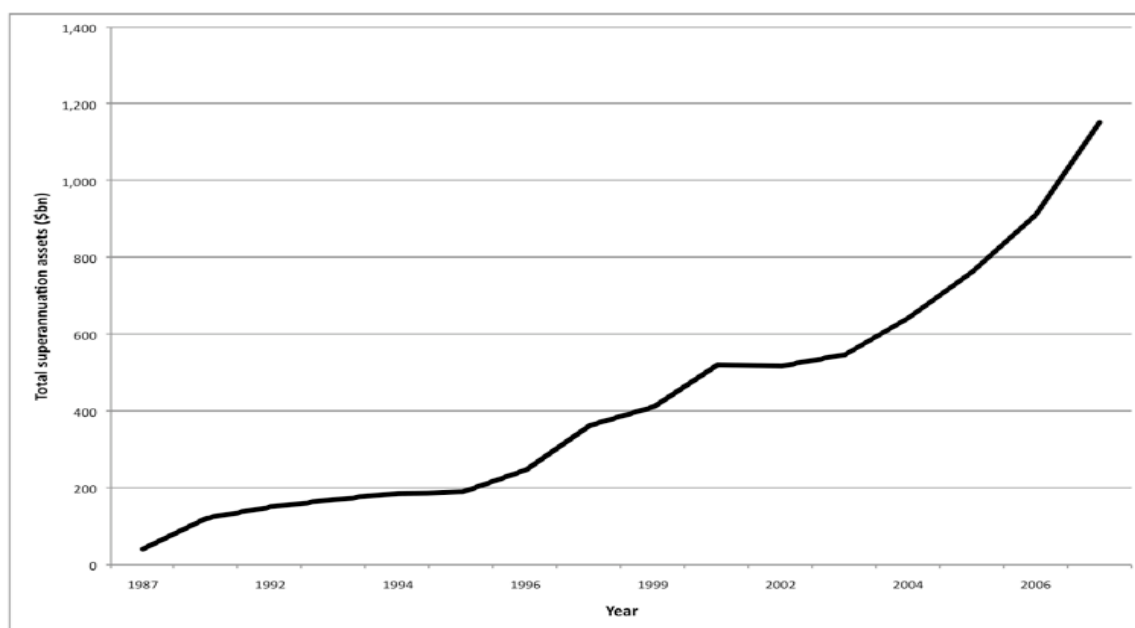


Table 7: Total superannuation assets

⁷⁰ Senate Select Committee, Parliament of the Commonwealth of Australia, *Safeguarding Super, the Regulation of Superannuation* (1992).

Whilst the increased amounts invested in superannuation funds reflected the success of the SG, the introduction of self managed funds in 1999 also contributed to the substantial increase of assets in superannuation funds.

Table 8 shows the increase in the number of self managed funds from 2003 while a decrease in total number of other superannuation funds.⁷¹ ‘Other Funds’ include public offer superannuation funds, non public offer superannuation funds, exempt schemes, approved deposit funds, eligible rollover funds, small APRA funds and pooled superannuation trusts.

Year	Number of self managed superannuation funds	Number of other funds
2003	253,559	11,055
2004	273,369	9,997
2005	289,990	8,754
2006	308,681	7,831
2007	349,636	6,843
2008	377,191	6,270
2009	401,929	4,934

Table 8: Number of self managed superannuation funds compared with the number of other superannuation funds

The decrease in the number of Other Funds coincides with the changes in the provisions of the legislation and the regulation of superannuation funds excluding self managed superannuation funds. A number of Other Funds amalgamated resulting in the total number of Other Funds decreasing.

Table 9 shows the proportion of assets accumulated in self managed superannuation fund from 2003 compared with other superannuation funds.

⁷¹ APRA, ‘Statistics’ (2009) *Annual Superannuation Bulletin* 29.

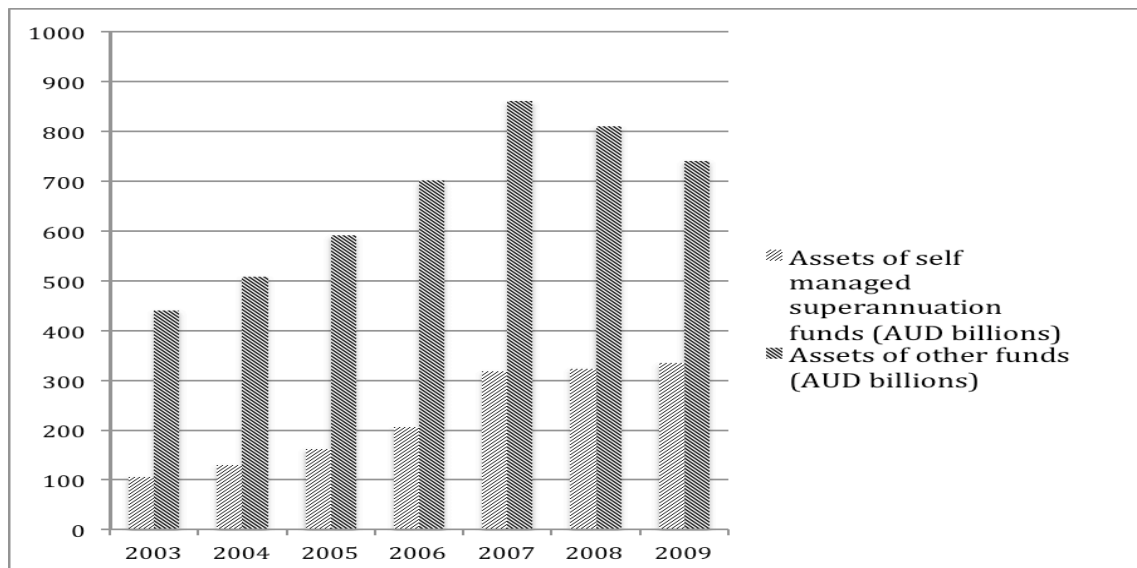


Table 9: Assets of self managed superannuation funds compared with the assets of other superannuation funds⁷²

The effects of the Global Financial Crisis are reflected in the decrease in the value of the assets held by Other Funds.

As at 30 June 2009, self managed superannuation funds held the largest proportion of superannuation assets, accounting for 31 per cent of total assets.

1.3.4 Simplifying Super

In October 2005, the Federal Government⁷³ announced the appointment of a Regulation Taskforce to identify actions to address areas of Australian Government regulation that ‘are unnecessarily burdensome, complex, redundant, or duplicate regulations in other jurisdictions’. The main focus was not on policy, but rather on any undue costs for business in the implementation of policy through regulation.

⁷² Ibid 37.

⁷³ The Liberal-Country Party coalition government under Prime Minister the Rt Hon John Winston Howard.

In a report, the Taskforce highlighted the need to simplify the taxation rules relating to superannuation in a report.⁷⁴ One of the Taskforce's major recommendations was that: '[t]he Australian Government should give high priority to comprehensive simplification of the tax rules for superannuation.'⁷⁵

As part of the 2006-07 Budget, the Treasurer released 'A Plan to Simplify and Streamline Superannuation'. Under this plan, Australians aged 60 and over should not pay tax on their superannuation benefits from 1 July 2007. As superannuation benefits would no longer be assessable income, there would be an incentive to continue to work while drawing down on superannuation.⁷⁶ The reforms were designed and introduced⁷⁷, inter alia, to improve incentives to save for retirement, increase retirement incomes and strengthen incentives for older Australians to stay in the workforce.

The strategy developed by the Federal Government to implement its retirement income policy was designed to encourage people to save for their retirement and to provide confidence in the superannuation system. The tax incentives for contributions and concessional tax treatment of income of superannuation entities coupled with the compulsory contributions for employees and the prospect of having tax free income in retirement provided people with the opportunity to save and plan for their retirement.

⁷⁴ Australian Government, Task Force on Reducing Regulatory Burdens on Business, *Rethinking Regulation* (2006).

⁷⁵ Ibid 128, recommendation 5.51.

⁷⁶ *SISR* reg 6.01 (definition of 'transition to retirement income stream' as an account-based income stream meets the standards in regs 1.05(11A) and 1.06(9A) and that limits the total amount of the payments in any year to no greater than 10% on the account balance at the start of each year). *SISR Sch 1 Conditions of Release of Benefits* item 110 attaining preservation age (a) a transition to retirement income stream.

⁷⁷ *Tax Laws Amendment (Simplification Superannuation) Act 2007*, No 9 2007.

1.4 Government's reaction and regulation

In response to the Federal Government's request for an enquiry into certain aspects of the taxation laws,⁷⁸ in 1961, the Ligertwood Report recommended that the provisions for superannuation funds established for the benefit of employees allowing the exemption of income from income tax in the *ITAA* be amended.⁷⁹ New provisions were inserted into the *ITAA* with the former provision repealed. The new provisions attempted to be specific in their application.⁸⁰

During the 1970s and the early 1980s, Australia experienced an increase in the application of tax avoidance⁸¹ techniques. The tax incentives available to the superannuation industry attracted the attention of the promoters of tax avoidance arrangements.⁸² The Federal Government was concerned about the public cost that tax concessions might have in the form of net reduced revenue

⁷⁸ The Liberal-Country Party coalition government under Prime Minister the Rt Hon Robert Gordon Menzies KC (later Sir Robert KT CH QC).

⁷⁹ Commonwealth Committee on Taxation, Commonwealth Government of Australia, *Report of the Commonwealth Committee on Taxation* (1961) xx, 154-7 [737]-[744].

⁸⁰ *ITAA* s 23F - exemption of income of superannuation funds established for the benefit of employees, as inserted by amendment *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, as repealed by *Income Tax Assessment Bill 1965*, No 103 1965. Substituted s 23F, as inserted by *Income Tax Assessment Bill 1965*, No 103 1965.

⁸¹ Prior to the restructuring of the provisions of the *ITAA* relating to the superannuation industry, the phrase 'tax avoidance' had been judicially held not to imply any conscious wrong doing on the part of the taxpayer but merely the payment of less tax than required. In *FC of T v Westgarth* (1950) 4 AITR 429 440, Fullagar J. stated 'The word "avoidance" is, I think, to be contrasted with the word "evasion". It involves, I think, no notion of escaping by any device or artifice, but conveys simply the notion of actually escaping through not being called upon to pay.'

G Lehmann & C. Coleman, *Taxation Law in Australia*, (LBC Information Services 4th ed, 1996), 852 – 853 [8.10]: 'Tax avoidance is the minimisation of tax through legal means which are artificial and contrived and have no rationale other than obtaining a tax benefit.'

⁸² One technique was the establishment of internal employer-sponsored superannuation funds to provide superannuation benefits for employees by their employer and managed by their employer. The employer had the advantages of the tax concessions for contributions to superannuation funds. Generally, these contributions to such a fund were tax deductible for the employer. The income received by these funds was exempt from income tax under certain conditions. The money could be lent back to the employer. The superannuation fund could invest in the employer. The employees may or may not have received the benefits.

collected⁸³ ie the cost of tax concessions less the cost of supporting the retired population.

To develop strategies to implement its policies, the Federal Government appointed committees to advise on issues. Sometimes the terms of reference were general and sometimes with specific focus. It sought advice on the superannuation industry and specifically the means to encourage saving for retirement and old age and to protect members' benefits.⁸⁴

⁸³ The Asprey Report, see below n 84, 31 [3.5].

⁸⁴ The committees appointed between 1936 and the introduction of *OSSA* that included recommendations relating to superannuation were:

- Commonwealth Committee on Taxation, Commonwealth Government of Australia, *Report of the Commonwealth Committee on Taxation* (1961). 'Ligertwood Report'.
- Taxation Review Committee, Commonwealth Government of Australia, *Full Report* (1975), 'Asprey Report'.
- Committee of Inquiry, Commonwealth Government of Australia, *A National Superannuation Scheme for Australia* (1976), 'Hancock Report Part One'.
- Committee of Inquiry, Commonwealth Government of Australia, *Occupational Superannuation in Australia* (1977), 'Hancock Report Part Two'.
- Committee of Enquiry, Commonwealth Government of Australia, *Australian Financial System* (1981). 'Campbell Report'.
- Commonwealth Taskforce, *Occupational Superannuation* (Parliamentary Paper No 27, Parliamentary Library, Commonwealth Government of Australia, 1983). 'Task Force Report'.

The committees appointed after the introduction of *OSSA* and before *SISA* were:

- Social Security Review, 'Towards a National Retirement Incomes Policy' (Issues Paper No 6 Commonwealth of Australia 1988);
- Senate Select Committee, Parliament of the Commonwealth of Australia, *Safeguarding Super, the Regulation of Superannuation* (June 1992); *Safeguarding Super the Regulation of Superannuation* (June 1992); *Super Guarantee Bills* (June 1992); *Super and the Financial System* (October 1992); *Super – Fiscal and Social Links* (December 1992); *Super Fees, Charges and Commissions* (June 1993); *Super Supervision Bills* (June 1993); *Super Complaints Tribunal* (October 1993); *Super Regs I* (August 1994); *Super Regs II* (November 1994); *Review of Superannuation Complaints Committee* (April 1996).
- *Financial System Inquiry Final Report* (1997);
- *Report of the Superannuation Working Group on Options for Improving the Safety of Superannuation* (2002).

The committees appointed to review the regulation of superannuation funds but not included in this thesis are:

- The Taxation Review Panel, *Australia's Future Tax System Report to the Treasurer* (2009);
- The Superannuation Review Panel, *Review of the Governance, Efficiency, Structure and Operation of Australia's Superannuation System* (2010).

After considering a number of reports from Committees appointed by the governments of the day, the Federal Government recognised the need for the restructuring of the superannuation industry, specifically regulating the application of the provisions within the *ITAA* relating to superannuation.

In 1984, as part of the strategy relating to its retirement policy in response to recommendations of a number of Committees, the Federal Government implemented a new taxation arrangement for retirement and kindred payments effective for payments made on or after 1 July 1983. As part of this strategy, approved deposit funds ('ADF') were introduced to act as investment vehicles designed to protect eligible termination payments⁸⁵ ('ETP') deposited in the care of the ADFs' trustees for a limited period.

The restructuring of the regulation of the Superannuation Industry commenced with the introduction of the *Occupational Superannuation Standards Act 1987* ('OSSA')⁸⁶ and Regulations ('OSSR')⁸⁷. OSSA commenced on 21 December 1987, but in most respects was deemed to apply from 1 July 1986. OSSA set out the requirements that superannuation funds and trusts had to comply with to be eligible for concessional tax treatment. It applied to all superannuation funds and ADFs whose trustees planned for their funds to qualify for income tax concessions.

The Australian Taxation Office ('ATO') regulated superannuation funds under provisions of *ITAA* from 1936 to 30 June 1986. On 1 July 1986, the Insurance and Superannuation Commission ('ISC')

⁸⁵ *ITAA* s 72A(1) defined 'eligible termination payments' to include retirement, termination and similar payments in consequence of the termination of a taxpayer's employment (including office). Superannuation fund payments were included, except those in the form of a pension or annuity.

⁸⁶ *Occupational Superannuation Standards Bill 1987*, No 97 1987, Date of Royal Assent on 5 November 1987, proclaimed in accordance with s 2 to commence on 21 December 1987. Transitional provisions deemed to apply from 1 July 1986.

⁸⁷ Commonwealth of Australia, *Occupational Superannuation Standards Regulations*, Statutory Rules 1987 No 322, 22 December 1987.

was established to regulate the administration and operations.⁸⁸ The Commissioner of Taxation retained the tax assessment role in relation to superannuation funds and also retained responsibility for allowing deduction for contributions to funds.⁸⁹

From 1 July 1988, funds were subject to tax, but, if the fund qualified as a complying superannuation fund or ADF, as defined in *ITAA* s 267, it was taxed at a concessional rate.⁹⁰ Complying superannuation funds and ADFs were those that satisfied standards set down in the *OSSA*.

As part of the new arrangements for the taxation of superannuation funds and approved deposit funds introduced in 1988, the Federal Government introduced a new type of fund, 'pooled superannuation trust' ('PST') to act as investment vehicles for complying superannuation and approved deposit funds.⁹¹ A PST is defined in a similar way to a complying superannuation fund but by reference to the trust obtaining a notice under section 15B or 15C of the *OSSA*.⁹²

From 1 July 1994, the *Superannuation Industry (Supervision) Act 1993* ('*SISA*')⁹³ replaced *OSSA*. *SISA* provided for the prudential management of superannuation entities. The *OSSA* was amended

⁸⁸ *Insurance and Superannuation Commissioner Bill 1987*, Nos. 98 1987.

⁸⁹ *Taxation Laws Amendment Bill (No 4) 1987*, No 138 of 1987.

⁹⁰ *ITAA* Part IX ss 267-315, as inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989.

⁹¹ *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989 applicable to assessments for the year of income in which 1 July 1988 occurred and all subsequent years.

⁹² *ITAA* s 267(1).

⁹³ The *Superannuation Industry (Supervision) Act 1993*, No 78 1993, as assented to on 30 November 1993, commenced on 1 December 1993, except Pt 1, 2, 21, 27-32, 30 November 1993; Pt 1 as it relates to s 117, 21 October 1992; Pt 18-20, 22-24, s 342, 1 July 1994.

with some sections repealed and renamed *the Superannuation Entities (Taxation) Act 1987*.⁹⁴

From 1 July 1998, Australian Prudential Regulation Authority ('APRA') replaced the ISC.⁹⁵ APRA was established to take responsibility for the supervision of banks, life and general insurance companies and superannuation entities.⁹⁶ The Commissioner of Taxation continued to retain the tax assessment role in relation to superannuation entities and also retained responsibility for allowing deductions for contributions to funds.

On 1 July 2000, the regulation of superannuation funds that complied with the definition of self-managed superannuation funds was transferred from APRA to the ATO.⁹⁷

In 2004, the introduction of licensing of trustees of superannuation entities (not trustees of self managed superannuation funds) had consequences that affected their regulation. The superannuation entities had to be registered with APRA. The *Corporations Act 2001* ('CA') was amended to include superannuation interests as financial products.⁹⁸ This meant that the trustees of superannuation entities had to comply with the disclosure and reporting requirements of the CA. ASIC assumed responsibility for market integrity and consumer protection across the financial system.

In 2007, changes relating to taxation of superannuation entities were minor with additions to the law clarifying or complementing the operation of the superannuation entity taxation provisions.

⁹⁴ *Occupational Superannuation Standards Amendment Act 1993*, No 84 1993.

⁹⁵ *Financial Sector Reform (Amendments and Transitional Provisions) Act 1998*, No 54 1998.

⁹⁶ *Australian Prudential Regulation Authority Act 1998*, No 50 1998.

⁹⁷ *Superannuation Legislation Amendment Act (No 3) 1999*, No 121 1999.

⁹⁸ CA s 764A(g) includes a superannuation interest, as defined by the *SISA*, as a financial product.

This background shows that there has been a substantial increase in the retirement population and that is continuing in an upward trend. It also shows that the Federal Government reacted to this increase by developing strategies to increase savings for retirement income. The legislation governing the regulation of superannuation has gone through multiple iterations since the first allowable deduction for a contribution to a fund established for retirement was introduced in 1915. Given the changes in regulation and the size of the retiree population, it is important to analyse whether there is consistent policy intent behind superannuation regulation, for without such consistency there is a very real danger of policy failure given the extensive time periods necessary to engineer superannuation provisions.

1.5 Hypothesis

The evolution of the legislation regulating superannuation funds has been consistent with the Federal Government's policy intent to encourage people to save for their own retirement. The Federal Government has implemented its policy by amending the legislation regulating superannuation funds to protect the members' benefits for their retirement and ensure the members' entitlements are available when required. It has made trustees of superannuation funds accountable for their responsibilities and included provisions within the legislation to prevent abuse of the superannuation system.

1.6 Methodology

Although there is substantial economic and social analysis, there is no disciplinary equivalent underpinning the evolution of superannuation regulation in Australia. The literature on the provisions that apply to superannuation entities generally focuses

on describing to superannuation and tax practitioners how changes to the laws will affect them and their clients.⁹⁹

Superannuation regulation was a product of a series of events. Its evolution resulted from the Federal Government's need to implement its retirement income policy and to protect members' benefits and its Revenue. This thesis is based on the analysis of the Federal Government's research of potential strategies for its retirement income policy and methodology for implementing them. In conducting the research for this thesis, in the absence of significant theory and almost any literature, use is made of judgments resulting from challenges by the Commissioner, reports to the Federal Government by Committees appointed for review of the legislation, policies, regulation and extrinsic materials. There is systematic exposition, analysis and critical evaluation of the regulation of superannuation, its implementation and historical development. Through this process, the thesis examines what is a major policy initiative with potentially massive budgetary implications for future government Revenue. This thesis aims to fill part of that gap in the analytical literature.

The thesis uses a qualitative methodological approach in the form of exposition, analysis and critical evaluation. The thesis proves the hypothesis through a mix of deductive and inductive reasoning from the regulation, cases and comprehensive reviews. The methodology follows what McKerchar describes as 'doctrinal research'¹⁰⁰. Accordingly, as it takes a broadly positivist approach,

⁹⁹ Examples: Andrew Fairley, 'The New Superannuation Regime – How the Occupational Standards Work' (1988) 62 (3) *Law Institute Journal* 146-151; Garry Beath, 'Occupational Superannuation Standards Set' (1988) *Law Society Journal* 20-1; Noel Davis, 'Income Tax Amendments – Superannuation' (1988) 22 *Taxation in Australia* 474-8; Ian Esdaile, 'The Long Awaited Relocation Regulations' (1990) 2 (4) *CCH Journal of Australian Taxation* 78-9; Noel Davis, 'Some Administration Issues' (1993) 6 (4) *Australian Superannuation Law Bulletin* 38-9; Jan Esdaile, 'Breaches, Bankruptcy and Money' (1993) 5 (5) *CCH Journal of Australian Taxation* 37-9.

¹⁰⁰ Margaret McKerchar, *Design and Conduct of Research in Tax, Law and Accounting* (2009) 115. This approach is described more generally in T Hutchinson, *Researching and*

the hypothesis is propositional, in that the evidence from cases, legislation and government reviews is used to ascertain its validity.¹⁰¹ However, although the thesis is largely doctrinal, the framework of non-doctrinal principal is acknowledged as critical in determining its nature.¹⁰² This is evidenced by the social and economic factors influencing the development of superannuation regulation,

The thesis provides a significant additional contribution to knowledge in that it is the only comprehensive study of the history of the regulation of superannuation. As such it provides a detailed analysis of the development of regulation not otherwise available. Enright and Sidorko identify the inadequacy of primary and secondary sources of law as a major impediment to successful legal research.¹⁰³ This thesis provides an accurate record of primary and secondary sources, overcoming the problems identified by Enright and Sidorko of:¹⁰⁴

- poor layout and style;
- unavailability of reprints;
- problems with annotations and indexes;
- inaccessibility particularly of delegated legislation, detail and status of amendments, cases in tribunals and lower courts, and secondary materials; and
- misprints, errors and lost materials.

The product of the research, which provides the first accurate historical record of the materials, is provided in detail in the

Writing in Law (3rd ed, 2010). Legal Research can be contrasted with both general qualitative methodologies, see MQ Patton, *Qualitative Research and Evaluation Methods* (3rd ed 2002) and quantitative methodologies, see W Neuman, *Social Research Methods: Qualitative and Quantitative Approaches* (6th ed 2006).

101 McKerchar *ibid*.

102 McKerchar, *ibid* 116, encourages the recognition of the inter-relationship of doctrinal and non-doctrinal approaches in producing a more realistic solution to research problems.

103 CS Enright and P Sidorko, *Legal Research Technique* (2002) 354.

104 *Ibid*.

footnotes to allow subsequent researchers a comprehensive resource on which to draw.

1.7 Structure

In conducting the research, it was necessary to understand and document the origin and development of the regulation implementing policy. Understanding the context and historical development provides the basis for analysis of the current position. It also provides a clear basis for determining whether the hypothesis can be proven. Without the historical context and understanding, there is insufficient basis for a complete analysis. The use in this thesis of a systematic historical analysis of the policy intent allows an assessment of the current position and ensures that recommendations about future policy are fully informed.

Chapter 2 provides information about legislation and interpretation pivotal to analysis and understanding the evolution of the regulation of superannuation funds.

Chapter 3 addresses the role of taxation in the Federal Government's policy to encourage people to save for their own retirement. Whilst the taxation and regulation of superannuation funds are related, the legislation separated with the introduction of the *OSSA* and then ran parallel and each piece of legislation complemented the other. The subsequent substitution of the *SISA* for the *OSSA* maintained this complementary role. Together they assisted the Federal Government implement its policy to fund the retired population (or to fund retirement).

Chapter 4 analyses the regulation of superannuation funds in *ITAA* as it applies to superannuation funds established and maintained for employees, identifying the main ambiguities and inadequacies. This analysis is dependant on the ATO's memoranda, second

readings of the legislation to be introduced for enactment by Parliament and the judgments in the cases which resulted from the Commissioner disallowing the tax concessions provided by *ITAA*.

Chapter 5 analyses the regulation of superannuation funds in the *ITAA* that were not established by employers for employees. The Federal Government established these superannuation funds to encourage people who were not supported by employers making contributions on their behalf to save for their retirement.

Chapter 6 analyses the Reports of the Committees appointed by the Federal Government to review the superannuation industry. The Committees were required to identify anomalies and inadequacies and to make recommendations for restructuring of the industry where appropriate. This Chapter assesses the *OSSA* and the *OSSR* and establishes that it rectified in part the ambiguities and inadequacies identified by the Boards of Review, the Courts and the Committees in the provisions of *ITAA* relating to the regulation of superannuation funds. It details how the measures introduced commenced the process of protecting the members' benefits. Analysis of the *OSSA* further highlights inadequacies that led to the appointment of Committees by the Federal Government to review the superannuation industry and the effectiveness of the *OSSA*. The Federal Government adopted the recommendation for substitution of the new legislation.

Chapter 7 provides analysis of *SISA* to establish if this legislation provides protection of members' benefits, making the trustees accountable for their responsibilities by the specifying of their obligations and duties and the imposition of penalties for non-compliance with the regulations. This analysis includes the role of the Authorities (ATO, APRA and ASIC), the Courts/Administrative Appeals Tribunal, the trustees, auditors and the penalty regime.

Chapter 7 proves the effectiveness of the *SISA* and the related legislation and the hypothesis that the Federal Government's policy intent to encourage people to save for their own retirement, make trustees accountable and prevent abuse has been successful.

Chapter 8 concludes the thesis by confirming that the evolution of the legislation regulating superannuation funds has been consistent with the Federal Government's policy intent to encourage people to save for their own retirement. It comments on the current position and makes a recommendation for the continuing implementation of the Federal Government's policy.

1.8 Limitations

This thesis does not, unless pertinent as supporting evidence to prove the hypothesis, analyse the regulation or taxation of contributions to, or benefits paid by, the trustee of a superannuation fund. It is restricted to the evolution of the regulation of superannuation entities. In the analysis of the regulation of the superannuation funds up to the introduction of the *OSSA*, the regulation of each type is reviewed to identify the issues and inadequacies in the regulations. In the analysis of superannuation entities after the introduction of the *OSSA* and the subsequent *SISA*, analysis is of the framework of the regulation, not the specifics of the provisions of legislation applicable to superannuation entities. There is extensive referencing in footnotes to the enactment of, insertion in and amendment of the legislation. This has been done to demonstrate the evolution of the regulation in the legislation. Also, each Federal Government appointing the various committees has been identified to demonstrate that there has been a bi-partisan approach to the retirement income policy and superannuation.

The analysis does not address the Federal Government's main objective of equity or protection of the Revenue unless pertinent to

the evolution of the regulation of superannuation funds nor the policy relating to its economic, social or overall revenue considerations. It is restricted to the period of saving by members in a superannuation fund, not the period of their retirement. It does not address the issue of reasonableness of members' entitlements in the context of quantifying or protecting the amount considered necessary for retirement.

1.9 Conclusion

Superannuation is a significant policy component of government regulation given the changing demographics and an increasing retired population. This thesis will show that the evolution of the legislation regulating superannuation funds has been consistent with the Federal Government's policy intent to encourage people to save for their own retirement. The Federal Government has implemented its policy by amending the legislation regulating superannuation funds to protect the members' benefits for their retirement and ensure the members' entitlements are available when required. It has made trustees of superannuation funds accountable for their responsibilities and included provisions within the legislation to prevent abuse of the superannuation system.

It will be shown that the framework evolved for the regulation of superannuation entities has been successful. The Federal Government was diligent in its research and consideration of the issues and inadequacies in the superannuation system. It has systematically implemented those recommendations of the Committees considered appropriate each time it introduced legislation for the regulation of superannuation funds.

Having provided the framework, whilst including penalties to prevent abuse to the system, the Federal Government is dependent

on the goodwill of the people and advisers and the efficiency of the Authorities to make it effective. It cannot legislate against greed and ignorance.

CHAPTER 2

'SUPERANNUATION FUND'

Faced with an ageing population, the Federal Government's retirement income policy was (and continues to be) to encourage people to save for their own retirement. To do this, it provided tax incentives. To access these tax incentives, taxpayers had to comply with provisions in the *Income Tax Assessment Act 1936* ('ITAA'). The increasing tax avoidance practices by taxpayers and their advisers made the development of a system to manage and secure these savings essential. The system had to promote the confidence of those involved in the system and ensure the availability of the savings on retirement for retirees. This was the basis for the evolution of the regulation of superannuation funds.

This Chapter describes the structure and the evolution of the interpretation of 'superannuation fund'. Initially 'superannuation fund' was not defined in the *ITAA*. The changes in the legislation regulating superannuation funds resulted in defining what the term meant for the specific legislation and regulations.

This Chapter underpins the analysis in subsequent chapters to prove the hypothesis. It provides an understanding of the structure of a superannuation fund and the pivotal role it plays in protecting members' benefits and making trustees accountable for their responsibilities. A superannuation fund provides the vehicle for protecting Revenue, the interests of those who invest and the beneficiaries.

2.1 Background

Prior to 1987, the *ITAA* simply referred to the exemption from income tax of income of 'a provident, benefit, superannuation or

retirement fund’.¹ It was the vehicle for contributions to be eligible for a tax deduction² and for exemption of its income from income tax³.

Rather than establishing a separate statutory entity, the Federal Government relied on trusts as the vehicle for superannuation funds. There existed a complete body of law that provided most of the requirements for fiduciary protection of assets invested for retirement. The vehicle generally used was a trust with trustee and trust deed to establish a superannuation fund. The various States of Australia enacted the law regulating the establishment and maintenance of trusts.⁴

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- ¹ ITAA s 23(j)(i) and substituted s 23F(1). ‘Retirement’ was added when s 23F replaced ITAA s 23(j)(i) in *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964.
- ² See Chapter 3 n 3, 4.
- ³ See Chapter 3 [3.2.1].
- ⁴ Acts current during 1936 to 1986:
 Trustee Act 1925 (New South Wales) Act No 14 1925, amended by Act No 204 1983, No 43 1984, Act No 1984;
 Trustee Companies Act 1964 (New South Wales) - Act No 6 1964, amended by Act No 82 1983.
 Trustee Act 1958 (Victoria) - Act No 6401 1958, amended by Act No 10048 1984, Act No 10087 1984, Act No 10143 1984, Act No 10168 1984;
 Trustee Companies Act 1964 (Victoria) - Act No 10168 1964.
 Trusts Act 1973-1981 (Qld) - Act No 24 1973, amended by Act No 72 1981;
 Trustee Companies Act 1968 - 1984 (Qld) - Act No 56 of 1968, amended *Gazette* 16 January 1981 103, Act No 57 1974, Act No 50 1975, Trustee Companies Act Amendment Act 1977, *Gazette* 24 December 1977 1688, Act No 40 1980, Act No 111 1981, ANZ Executors and Trustee Company Act 1983, *Gazette* 21 June 1983 1253, Act No 49 1984, *Gazette* 8 June 1985 1083.
 Trustee Act 1936 - 1984 (South Australia) - Act No 2270 1936, amended by Act No 55 1980, Act No 44 1982, Act No 111 1983, Act No 2 1984, Act No 49 1984;
 Trustee Act 1893 (South Australia) - By virtue of the Trustee Act 1936 - 1984 (SA) ss 30, 31, 32, 33, 34, 38, 39(2), 43, 35, 36, 69, 72, 73, 74, and 75 of this Act are still in force.
 Trustee Act 1962 - 1978 (Western Australia) Act No 78 1962.
 Trustee Act 1898 (Tasmania) - Act No 34 1898, amended by Act No 49 1979, Act No 47 1981, Act No 52 1982, Act No 65 1985;
 Trustee Companies Act 1953 (Tasmania) Act No 72 1953, amended by Act No 36 1958, Act No 29 1959, Act No 7 1960, Act No 7 1961, Act No 66 1962, Act No 63 1963, Act No 55 1965, Act No 48 1967, Act No 25 1970, Act No 117 1973, Act No 91 1975, Act No 67 1978, Act No 74 1978, Act No 9 1982, Act No 74 1985.
 Trustee Ordinance 1957 (Australian Capital Territory) - Ordinance No 14 1957, amended by Ordinance No 18 1968, Ordinance No 28 1975, Ordinance No 46 1978, Ordinance No 27 1982, Ordinance No 9 1985;
 Trustee Companies Ordinance 1947 (Australian Capital Territory) - Ordinance No 15 1947, amended by Ordinance No 14 1954, Ordinance No 16 1954, Ordinance No 7 1960,

Lindly LJ said that trusts were 'equitable obligations to deal with property in a particular way'.⁵ A more complete description of a trust is:

... an obligation enforceable in equity which rests on a person (the trustee) as owner of some specific property (the trust property) to deal with that property for the benefit of another person (the beneficiary) or for the advancement of certain purposes.⁶

An Act of Parliament, an agreement or set of rules or regulations or a life assurance policy, linked to a trust deed or provisions, could also establish a superannuation fund. These types of fund were either 'public sector funds' or those established by assurance companies as part of their superannuation business.

A trust under the legislation regulating trusts has four elements.⁷ These are:

1. a trustee who holds a legal or an equitable interest in the trust property;
2. property capable of being held on trust;
3. a beneficiary;⁸ and
4. a personal obligation which is annexed to the property.

In the context of a trust as a superannuation fund, on the establishment of a superannuation fund:

1. the employer⁹ agrees to pay an amount or amounts to the trustee¹⁰;

Ordinance No 19 1961, Ordinance No 7 1962, Ordinance No 11 1962, Ordinance No 4 1965, Ordinance No 12 1966, Ordinance No 19 1966, Ordinance No 8 1968, Ordinance No 93 1982, Ordinance No 6 1984.

⁵ *Re Williams* [1897] 2 Ch 12, 18, cited by Isaacs J in *Glenn v Federal Commissioner of Land Tax* (1915) 20 CLR 490, 503.

⁶ HAJ Ford & WA Lee, *Principles of the Law of Trust* (Law Book Company, 1983) 3.

⁷ R P Meagher QC and W M C Gummow, *Jacobs' Law of Trusts of Australia* (Butterworths 5th ed, 1986) 8.

⁸ *Ibid.* The trustee himself may be one of the beneficiaries, but he cannot be the sole beneficiary.

⁹ The settlor under trust law.

¹⁰ The first trustee is named in and signs the deed.

2. the trust property is all future contributions received and all income from investments made by the trustee; and
3. those who become members of the fund are the beneficiaries of the trust.¹¹

The deed of trust for a superannuation fund sets down:

1. the rights and obligations of the parties;
2. the conditions of the fund, eg eligibility for membership, contributions, the kind¹² and level of benefits, the payment of benefits; and
3. the way the fund would comply with legislation.¹³

The Right Honourable Lord Browne-Wilkinson noted the differences between traditional and superannuation trusts. The differences in superannuation funds are:

- beneficiaries are not volunteers;
- there is an underlying contract of employment;
- the size of the trust is variable;
- the employer continues to have a financial interest; and
- the trustees have power to amend the scheme.¹⁴

Lord Browne-Wilkinson concluded that trusts were the appropriate entity for superannuation funds because ‘the rules of equity which impose strict limits on the powers and duties of trustees provide protection for the beneficiaries.’ However, the ability to amend the

¹¹ See Chapter 4 [4.2.1].

¹² Funds could be allocated or unallocated and payments could be as a pension or a lump sum payment or a combination of both depending on the terms and conditions of the trust deed. They could also be ‘accumulation funds’ or ‘defined benefit funds’, originally known as ‘benefit promised scheme’. Accumulation funds were funds in which the member’s entitlement at retirement or resignation was not defined in amount in the deed but was represented by the accumulation of contributions made on the member’s behalf plus interest thereon. A ‘defined benefit fund’ had the benefits defined in the superannuation deed.

¹³ See above n 11.

¹⁴ Rt Hon Lord Browne-Wilkinson, ‘Equity and its Relevance to Superannuation Today’ (Paper presented at the National Conference for Lawyers: Trusteeship Issues under a Magnifying Glass on Superannuation, February 1992) 1.5-1.11.

general rules of a superannuation fund to include express powers authorising transactions prohibited by the general rules of equity potentially exposed members' interests to greater risks.¹⁵

2.2 The definition for the *ITAA*

ITAA s 23(j) provided the original exemption from income tax for income of various types of funds.¹⁶ It referred to funds established for special purposes. To be eligible for exemption, a fund had to be applied for the purpose for which it was established. The subsections implied that monies contributed to a fund must be held on trust for that purpose if the fund was going to be eligible for exemption. *ITAA* s 23(j)(i) exempted income from income tax if a fund was established and applied for the benefit of employees. *ITAA* ss 23F and 23(jaa) were substituted for *ITAA* s 23(j)(i). They were effectively a continuation of the exemption previously conferred under the more general provision of the *ITAA* s 23(j)(i) with 'superannuation fund' being defined as 'a provident, benefit, superannuation or retirement fund'.¹⁷

Because there was no definition of 'superannuation' or 'superannuation fund' within the *ITAA* prior to the introduction of the *Occupational Superannuation Standards Act 1987* ('OSSA')¹⁸, Windeyer J said in *Associated Provident Funds Pty Limited v FC of T*¹⁹, that the 'meaning of the term must ... depend upon ordinary usage'. In *Mahoney v FC of T*²⁰, Kitto J in the Full Court of the High Court also held this view.

Depending on ordinary usage, a definition of superannuation fund could be developed as follows. To superannuate means 'to declare

¹⁵ Ibid 1.10-1.11.

¹⁶ See Chapter 3 [3.2.1].

¹⁷ See Chapter 4 [4.3]-[4.4].

¹⁸ *Occupational Superannuation Standards Act 1987*, No 97 1987.

¹⁹ (1966) 14 ATD 333 351.

²⁰ (1967) 14 ATD 519 520.

too old for work²¹, ‘to send into retirement²² with pension²³ and ‘to allow to retire²⁴ from service or office on a pension on account of age or infirmity²⁵. ‘Superannuation’ is a pension²⁶ or allowance²⁷, ie a benefit²⁸, paid to a superannuated person.²⁹ ‘Fund’, a generic term as compared with the specific term ‘money’, is ‘a stock of money or pecuniary resources, as for some purpose’.³⁰ Windeyer J. in *Associated Provident Funds Pty Ltd v FC of T*³¹ stated that a ‘fund’, in the context ‘superannuation fund’, ordinarily meant money (or investments) set aside and invested, the surplus income therefrom being capitalised. His Honour said this was a general description. ‘Provident’ is defined as ‘providing carefully for the future’.³²

In summary, a superannuation fund depending on ordinary usage meant a fund comprising assets accumulated, with income of the fund capitalised, for the specific purpose of providing a pension or allowance to a retired person or persons.

21 H W Fowler and F G Fowler (eds), *The Oxford Dictionary*, (Oxford at the Clarendon Press 5th ed. 1964) 1296.

22 Ibid 1064 ‘seclusion, privacy, secluded place’.

23 Ibid 1296.

24 Ibid 1064. To retire means to ‘cease from or give up office or profession or employment or candidature’.

25 A Delbridge and JRL Bernard (eds), *The Concise Macquarie Dictionary*, (Doubleday 1982) 1294.

26 Ibid 926. ‘Pension’ defined as a ‘fixed periodical payment made in consideration of past services, injury or loss sustained, merit, poverty, etc.’.

27 Ibid 41. ‘Allowance’ defined as a ‘definite sum of money allotted or granted to meet expenses or requirements’, eg lump sum payment.

28 The Oxford Dictionary, see above n 21. ‘Benefit’ defined as ‘allowance’, ‘pension’ 110.

29 The Concise Macquarie Dictionary, see above n 25, 1294.

30 J Stein and L Urdang (eds), *The Random House Dictionary of the English Language*, (Random House, Unabridged Edition, 1966) 574.

H C Black, *Black’s Law Dictionary*, (St Paul Minn, 6th ed, 1990) 673 (definition of ‘fund’ meant ‘a sum of money and/or other liquid assets set apart for a specific purpose, or available for the payment of general debts, claims or expenses’).

H A J Ford, G W Hinde, M S Hinde, *Australian Business Dictionary*, (Butterworths, 1985) 113 (definition of ‘liquid assets’ meant assets that can be easily and quickly exchanged for cash).

31 (1966) 14 ATD 333, 351.

32 The Random House Dictionary, see above n 30, 1157.

During the 1970s and 1980s, inadequacies in the *ITAA*³³ led to a government response with amendments to the legislation and the prudential supervision. With the amendments in the legislation, the type of trust used for superannuation funds evolved into a 'statutory' trust designed more specifically to give effect to superannuation policy. The amended legislation assisted the trustees of superannuation funds, the Commissioner of Taxation and judiciary in their interpretation of its application. It provided some protection for members' interests and made trustees accountable for their responsibilities.

Compliance by the trustee of a superannuation fund with the statutory definition of a 'superannuation fund' was essential for the fund to be eligible for the relevant tax concessions. With the changes in the regulation of superannuation funds, consequential changes were made in the complementary acts and regulations.³⁴

2.3 The definition for the *OSSA*

For a superannuation fund to be eligible for concessional tax treatment, it had to comply with the provisions of the *OSSA*.³⁵ The *OSSA* was the specialist legislation introduced in 1987 to regulate the establishment and maintenance of superannuation funds.³⁶ *Occupational Superannuation Standards Regulations* ('*OSSR*')³⁷ prescribed the various operating standards and operating definitions for the implementation of the *OSSA*.

³³ See Chapters 4 [4.3.5.1], 5.

³⁴ See Chapter 3 [3.2].

³⁵ *ITAA* s 6(1), as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987, effective 18 December 1987, (definition of superannuation fund included '(a) a superannuation fund within the meaning of the *Occupational Superannuation Standards Act 1987*; and (b) a fund to which section 23 FC applies in relation to the year of income concerned').

After the introduction of *ITAA* pt IX on 1 July 1988, a superannuation fund had to be a 'complying superannuation fund', ie comply with the provisions of the *OSSA*.

³⁶ See Chapter 6.

³⁷ Commonwealth of Australia, *Occupational Superannuation Standards Regulations*, Statutory Rules No 322, 22 December 1987.

The O SSA included a definition of 'superannuation fund'. Initially a superannuation fund was:

a fund that:

- (a) is an indefinitely continuing fund; and
- (b) is maintained solely for either or both of the following purposes:
 - (i) the provision of benefits for each member of the fund in the event of the retirement of the member from any business, trade, profession, vocation, calling, occupation or employment in which the member is engaged;
 - (ii) the provision of benefits for dependants of each member of the fund in the event of the death of the member;or for either or both of those purposes and for such ancillary purposes as the Commissioner approves;³⁸

Prior to 1 July 1990, benefits had to be payable only on the member's retirement from a business, trade, profession, vocation, calling, occupation or employment in which the member had been engaged.

From 1 July 1990, paragraph (b) of the definition of superannuation fund was amended to read that a superannuation fund was maintained solely for one or more of the following purposes:

- (i) ...
- (ii) the provision of benefits for each member of the fund in the event of the member attaining a particular age (being an age not less than the age prescribed by the regulations) without having retired from any business, trade, profession, vocation, calling, occupation or employment in which the member is engaged;
- (iii) the provision of benefits for dependants of each member of the fund in the event of the death of the member, being a death occurring before:
 - (A) the member's retirement from any business, trade, profession, vocation, calling, occupation or employment in which the member is engaged;

³⁸ O SSA s 3(1).

- (B) the member attains a particular age (being an age not less than the age prescribed for the purposes of subparagraph (ii)) without having retired from any business, trade, profession, vocation, calling, occupation or employment in which the member is engaged;
- whichever is earlier;
-³⁹

From 22 December 1992, the definition of 'superannuation fund' was amended to allow more flexibility by permitting retired people to transfer their pensions from one provider to another.

- ...
- (iv) the provision of pensions for each transferred retiree member of the fund;⁴⁰

2.4 The definition for the *SISA*

Superannuation Industry (Supervision) Act 1993 ('*SISA*') in 1993 replaced the *OSSA*, the law regulating the establishment and maintenance of a superannuation fund.⁴¹ The Federal Government introduced the *SISA* to increase the level of prudential protection provided to the superannuation industry, to minimise risks associated with the investments in the superannuation industry and to protect the rights of superannuation fund members.⁴²

The *SISA* defines a superannuation fund to mean:

- (a) a fund that:
- (i) is an indefinitely continuing fund; and
 - (ii) is a provident, benefit, superannuation or retirement fund; or

³⁹ *Occupation Superannuation (Reasonable Benefit Limits) Amendment Bill 1990*, No 61 1990, effective 1 July 1990 paragraph (b)(ii), (iii) was substituted for (b)(ii).

⁴⁰ Paragraph (b)(iv), as inserted by *Taxation Laws Amendment (Superannuation) Act 1992*, No 208 1992.

⁴¹ *Superannuation Industry (Supervision) Act 1993*, No 78, 1993, Date of Royal Assent 30 November 1993, commencement generally 1 December 1993.

⁴² Minister for Higher Education and Employment Services and Minister Assisting the Treasurer, P Baldwin, 'Superannuation Industry (Supervision) Bill 1992' (Second Reading Speech at the House of Representatives, Canberra, Wednesday 16 December 1992).

- (b) a public sector superannuation scheme.⁴³

Whilst the definition of superannuation fund reverts back to the language in the *ITAA*⁴⁴, ‘a provident, benefit, superannuation or retirement fund’, the provisions for the regulation of superannuation funds in the *SISA* define and clarify their application. This reduces the requirement for interpretation of the earlier sections that applied to superannuation funds.

The *SISA* defines a public sector superannuation scheme as:

a scheme for the payment of superannuation, retirement or death benefits, where the scheme is established:

- (a) by or under a law of the Commonwealth or the government of a State or Territory;
- (b) under the authority of:
 - (i) the Commonwealth or the government of a State or Territory;
 - or
 - (ii) a municipal corporation, another local governing body or a public authority constituted by or under a law of the Commonwealth or of a State or Territory.⁴⁵

For a superannuation fund to be eligible for concessional tax treatment of its income, it had to be a ‘complying superannuation fund’.⁴⁶ A superannuation fund is a complying superannuation fund if:

- the prudential Regulator has given a notice to the fund that it is a complying superannuation fund in relation to a year of income and has not subsequently given a notice to the fund that it is not a complying superannuation fund;⁴⁷ and

⁴³ *SISA* s 10(1).

⁴⁴ *ITAA* ss 23(j)(i), 23F.

⁴⁵ *SISA* s 10(1) (definition of ‘public sector superannuation scheme’).

⁴⁶ See Chapter 3 for analysis.

⁴⁷ *SISA* s 45.

- the superannuation fund was a resident regulated superannuation fund at all times during the year of income when it was in existence; and
 - the trustee did not contravene the *SISA* or *Superannuation Industry (Supervision) Regulation* ('*SISR*')⁴⁸ in relation to the fund in respect of the year of income; or
 - the trustee contravened the *SISA* or *SISR* in respect of the year of income on one or more occasions but the fund did not fail the culpability test⁴⁹ in relation to any of those contraventions.⁵⁰

For a superannuation fund to be a 'regulated superannuation fund', it must comply with the following:

1. it must have a trustee;
2. either:
 - (a) the trustee is a constitutional corporation as required by the fund's governing rules; or
 - (b) the governing rules provide that the sole or primary purpose of the fund is to provide old-age pensions; and
3. each trustee must give a written notice to the prudential Regulator, signed and in the approved form, electing that the *SISA* is to apply to the superannuation fund.⁵¹

The definition of superannuation in the *SISA* and additional definitions provided clarity for the application of the legislation relating to the regulation of the superannuation industry. These additional definitions were:

⁴⁸ Commonwealth of Australia, *Superannuation Industry (Supervision) Regulations*, Statutory Rules No 57, 4 March 1994.

⁴⁹ See Chapter 7 [7.2.6.3].

⁵⁰ *SISA* s 42(1).

⁵¹ *SISA* ss 10(1), 19.

- standard employer-sponsored fund - a regulated fund where there is at least one employer sponsor.⁵² An employer will be taken to be a standard employer-sponsor if they contribute to the fund for the benefit of an employee of the employer or an associate of the employer, or for the benefit of dependants of such an employee on their death;⁵³
- public offer superannuation fund - a regulated fund other than a standard employer-sponsored fund, or an employer-sponsored fund that has at least one member who does not receive the employer contribution and who is not a member of a prescribed class. In such cases, the trustee may elect that the fund be treated as a public offer fund. Once such an election is made, it may only be revoked by the Commissioner;⁵⁴
- superannuation entity - a superannuation fund, an approved deposit fund, or a pooled superannuation fund;⁵⁵
- ‘excluded superannuation fund’ meant a superannuation fund of which there are fewer than 5 members;⁵⁶
- self-managed superannuation fund replaced ‘excluded superannuation fund’ for a superannuation fund with fewer than 5 members.⁵⁷

2.5 Conclusion

The evolution of the definition of a superannuation fund was pivotal to the evolution of their regulation. Coupled with the evolution of specialist legislation and introduction of specialist bodies for the regulation of the superannuation industry, it

⁵² *SISA* ss 10(1), 16(3), (4).

⁵³ *SISA* ss 10(1), 16(2).

⁵⁴ *SISA* ss 10(1), 18.

⁵⁵ *SISA* s 10(1).

⁵⁶ *ITAA* s 10(1), (definition of ‘excluded superannuation fund’), as repealed by *Superannuation Legislation Amendment Act (No 3) 1999*, No 121 1999. See Chapter 6 for analysis.

⁵⁷ *SISA* ss 10(1), 17A. See Chapter 7 for analysis.

provided the structure for prudential protection, allowing protection of the rights and benefits of superannuation fund members and making trustees accountable for their responsibilities.

CHAPTER 3

TAXATION OF SUPERANNUATION FUNDS

Chapter 2 analysed the evolution of the original basic trust structure of a superannuation fund to a ‘statutory trust’ through examination of the changing definitions. The trust structure was integral to the policy initiative to protect members’ benefits. Also necessary were policy initiatives to encourage saving in the protected structures.

Initially, tax incentives were central to the Federal Government’s strategy for encouraging people to save for their own retirement. Over time, an additional strategy was introduced through compulsory contributions by employers for employees. The simultaneous imposition of tax on the income of superannuation funds was necessary to offset additional deductions provided for the compulsory contributions, the change to the taxation of members’ benefits and the increase in those dependent on the aged pension.¹

This Chapter outlines the concessional tax treatment of the income of superannuation funds. It will show that the initial strategy of tax incentives employed by the Federal Government was successful in encouraging people to save for their own retirement. These incentives coupled with the compulsory contributions by employers for employees resulted in significant superannuation coverage for employees and an increase in assets in superannuation funds.

3.1 Background

The regulation of superannuation funds was initially achieved through *Income Tax Assessment Act 1936* (‘ITAA’) in conjunction with the law regulating the establishment and maintenance of

¹ See Chapter 1 Table 4.

trusts enacted by the various States of Australia. With the evolution of the regulation of superannuation funds,² the provisions for taxation in the *ITAA* were amended to reflect the changes of the regulation.

During the evolution of the specialist role of the regulator of superannuation funds, the Commissioner of Taxation retained the tax assessment role. The income tax concessions remained a policy tool of the Federal Government to support and encourage self-funded retirement through superannuation. The provisions relating to the tax concessions evolved with the implementation of strategies to give effect to the Federal Government's retirement income policy. The three main categories of tax concessions available to superannuation to encourage saving included:

- deductions and rebates for contributions to superannuation funds – employer contributions³ and personal contributions⁴;

² *Occupational Superannuation Standards Act 1987* followed by *Superannuation Industry (Supervisions) Act 1993*. See Chapters 6 and 7 respectively for detailed discussion.

³ *ITAA* s 66 – deductions for contributions to pension funds by employers, as repealed by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. *ITAA* s 79 – deductions for voluntary contributions to pension funds by persons other than employers, as inserted by *Income Tax Assessment Act 1944*, No 3 1944. New s 79 (five per centum of cost of assets of superannuation fund established for employees and other persons to be allowable deduction) substituted by *Income Tax Assessment Act 1965*, No 103 1965. See below n 31.

ITAA pt III div 3 sub-div AA – Contributions to Superannuation Funds for Benefits of Employees - ss 82AAA-82AAR, as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, as repealed by *Superannuation Legislation Amendment (Simplification) Act 2007*, No 15 2007 applicable to the 2007-2008 income year and later years.

ITAA 97 pt 3-30 – Superannuation, as inserted by *Tax Laws Amendment (Simplified Superannuation) Act 2007*, No 9 2007, applicable to the 2007-2008 income year and later years. *ITAA* 97 pt 3-30 div 290 sub-div 290-B applies to employer contributions.

⁴ *ITAA* pt III div 17 – s 82H – 'Rebates' – s 160(f)(ii), as repealed by *Income Tax and Social Services Contribution Assessment Act 1950*, No 48 1950.

ITAA pt III sub-div B – 'Concessional Deductions', as inserted by *Income Tax and Social Services Contribution Assessment Act 1950*, No 48 1950, as repealed by *Income Tax Assessment Act (No 2) 1975*, No 117 1975.

ITAA pt III div 17 'Rebates' ss 159 N, 159R, as inserted *Income Tax Assessment Act (No 2) 1975*, No 117 1975. *ITAA* s 159R as amended by *Income Tax Assessment Amendment Act (No 4) 1980*, No 124 1980.

ITAA pt III div 3 sub-div AB – 'Contributions to superannuation funds by eligible persons' ss 82AAS-82AAT, as inserted by *Income Tax Assessment Amendment Act (No 4) 1980*, No 124 1980, as repealed by *Superannuation Legislation Amendment (Simplification) Act 2007*, No 15 2007 applicable to the 2007-2008 income year and later years.

- concessional tax treatment of benefits paid from superannuation funds to employees on retirement⁵; and
- exemption/concessional treatment of income derived by superannuation funds.⁶

As a deterrent, the regulations imposed penalties by withdrawing these concessions where there was non-compliance with the rules regulating superannuation funds.

It will be shown that the incentives of tax concessions were consistent with and supported the Federal Government's policy intent to encourage people to save for their own retirement.

3.2 Income Tax legislation

This thesis is restricted to the evolution of the regulation of superannuation funds. Unless relevant to the regulation of the operations of a superannuation fund by a trustee, no reference is made to contributions to and benefits paid by a superannuation fund.

For a superannuation fund, the exemption of income from income tax initially and later the imposition of the concessional rate of

⁵ ITAA 97 pt 3-30– Superannuation, as inserted by *Tax Laws Amendment (Simplified Superannuation) Act 2007*, No 9 2007, applicable to the 2007-2008 income year and later years. ITAA 97 pt 3-30 div 290 sub-divs 290-C, 290-D apply to personal contributions. ITAA s 26(d), omitted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

ITAA pf III div 2 sub-div A s 26AE: 'Assessable income to include 5% of certain superannuation benefits', as inserted by *Income Tax Assessment Amendment Act (No 4) 1980*, No 124 1980. Omitted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

ITAA pt III div 2 sub-div AA – 'Superannuation, termination of employment and kindred payments' – ITAA ss 27A - 27J, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984, as repealed by *Superannuation Legislation Amendment (Simplification) Act 2007*, No 15 2007 applicable to the 2007-2008 income year and later years.

ITAA 97 pt 3-30 div 301 – 'Superannuation member benefits paid from complying plans etc', as inserted *Tax Laws Amendment (Simplified Superannuation) Act 2007*, No 9 2007, applicable on and after 1 July 2007.

⁶ See text for details of provisions of the ITAA relating to the taxation of superannuation funds, [3.2.1], [3.2.2].

income tax on income depended on compliance by the trustee of the superannuation fund with provisions of the legislation regulating the fund.

The taxation of superannuation funds falls into two distinct periods. The first period is the period when the income of superannuation funds was exempt from income tax provided they complied with the relevant provisions in the *ITAA*. This period commenced on 2 June 1936 and ended 30 June 1988. The second period relates to when superannuation funds had concessional rates of tax applied to the assessable income including taxable contributions made to the fund. This period of taxation commenced 1 July 1988.

During the first period, limitations to the exemption were introduced. Some limitations extended into the second period. One limitation, introduced effective from 15 June 1961, involved the compulsory investment in public securities. This compulsory investment was known as ‘the 30/20 rule’.⁷ It was abolished on 11 September 1984 with effect from the commencement of that year of income.⁸

The ‘in-house asset rules’ were substituted commencing on 1 July 1985.⁹ These rules extended into the second period relating to the taxation of superannuation funds. The decision to implement these rules reflected the Federal Government’s concern, supported by Committees reviewing the superannuation system, that excessive investment by the trustee of a superannuation fund in the sponsoring employer’s business might mean, in the event of the

⁷ See [3.3.1].

⁸ Repealed by *Taxation Laws Amendment Act 1985*, No 49 1985.

⁹ See [3.3.2].

failure of that business, that employees lose not only their jobs, but also their superannuation entitlements.¹⁰

In 1964, in response to the recommendations of Report of the Commonwealth Committee of Taxation,¹¹ further limitations excluded certain income of superannuation funds from the exemption from income tax. Dividends received from private companies could only be included in the calculation of exempt income if the Commissioner considered it reasonable for the exemption to apply provided specific criteria were met. Also, income was excluded from the exemption if the parties to the transaction giving rise to the income were not dealing with each other at arm's length and the income was greater than that which might have been expected to have been derived from the transaction if those parties had been dealing at arm's length.¹²

In 1980, tax avoidance provisions were introduced to discourage the abuse of tax concessions by diverting income for example to superannuation funds.¹³

During the second period commencing on 1 July 1988, *ITAA* Part IX introduced the imposition of income tax on the income of

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- ¹⁰ 1. Taxation Review Committee, Commonwealth Government of Australia, *Full Report* (1975) 'Asprey Report' [21.101];
 2. Committee of Inquiry, Commonwealth Government of Australia, *Occupational Superannuation in Australia* (1977) 'Hancock Report Part Two' 104 [7.13];
 3. Committee of Enquiry, Commonwealth Government of Australia, *Australian Financial System* (1981) 'Campbell Report' 349 [20.126];
 4. Commonwealth Taskforce, *Occupational Superannuation* (Parliamentary Paper No 27, Parliamentary Library, Commonwealth Government of Australia, 1983) 'Task Force Report' 36 [4.30].
- ¹¹ Commonwealth Committee on Taxation, Commonwealth Government of Australia, *Report of the Commonwealth Committee on Taxation* (1961), 'Ligertwood Report' 156 [744].
- ¹² Inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. See [3.3.3].
- ¹³ See [3.2.1.2].
ITAA pt III div 9C, *Income Tax Laws Amendment Act 1981*, No 108 1981, commencement date 24 June 1980.

superannuation funds.¹⁴ Capital gains tax also applied to superannuation funds from 1 July 1988.¹⁵

In 1996, a surcharge was introduced on contributions made to superannuation funds, subject to an income threshold of the member. This was abolished in 2005.

In 2006, a government taskforce highlighted in a report the need to simplify the taxation rules relating to superannuation.¹⁶ As a result of the report, Part IX of *ITAA* was repealed and replaced by Part 3-30 Superannuation in *Income Tax Assessment Act 1997* (*ITAA 97*).¹⁷

Each period will be reviewed to analyse the application of tax concessions to the income of superannuation funds. Then, as two of the limitations to the application of tax concessions span the two periods,¹⁸ the three limitations are considered in detail. It will be shown that the policy developments were primarily focused on encouraging members to save for their own retirement, but without permitting loopholes that might diminish the policy effectiveness.

¹⁴ *ITAA* pt IX – Taxation of superannuation and related business, comprising ss 267-315, as inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989, as amended by *Taxation Laws Amendment (Superannuation) Act 1989*, No 105 1989, applicable to assessments for the year of income in which 1 July 1988 occurred and all subsequent years.

¹⁵ *ITAA* pt IIIA, as inserted by *Income Tax Assessment (Capital Gains) Act 1986*, No 52 1986.
ITAA div 115, sub-div 115-A provided discount capital gains to superannuation funds of *ITAA 97*, as inserted by *A New Tax System (Personal Income Tax Cuts) Act 1999*, No 169 1999. *ITAA 97* s 115-100 provided for a discount of 33.33% for superannuation funds compared with other eligible entities which were allowed a discount of 50%.

¹⁶ Australian Government, Task Force on Reducing Regulatory Burdens on Business, *Rethinking Regulation* (2006).

¹⁷ *ITAA* pt IX, as repealed by *Tax Laws Amendment (Simplified Superannuation) Act 2007*, No 9 2007 and replaced by *ITAA 97* div 295 applicable to the 2007-2008 income year and later years.

¹⁸ The in-house asset rules and the rules that apply to ‘special income’/‘non-arm’s length income’.

3.2.1 *The first period – exempt from income tax*

On 2 June 1936, the date of assent, the *ITAA* commenced.¹⁹ From 1936 to 1988, the income tax treatment that applied to superannuation was in the Federal income tax legislation²⁰. The Commissioner of Taxation ('Commissioner') had the general administration of the *ITAA*.²¹

Initially, for the tax treatment of income derived by superannuation fund, a general provision in the *ITAA* s 23(j)(i), provided exemption from income tax for superannuation funds providing benefits for employees:

the incomes of the following funds, provided that the particular fund is being applied for the purpose for which it was established -

- (i) a provident, benefit or superannuation fund established for the benefit of employees;

... .

From 1952, *ITAA* s 23(ja)²² exempted from income tax income of a provident, benefit, superannuation or retirement fund for self-employed persons where the fund complied with terms and conditions provided by *ITAA* and the Commissioner.

The *ITAA* defined 'exempt income' to mean 'income which is exempt from income tax and includes income which is not assessable'.²³

But for the specific exemption in relation to superannuation funds,

¹⁹ *Income Tax Assessment Act 1936*, No 27 1936, Date of Assent, commencement 2 June 1936.

²⁰ *Income Tax Assessment Act 1936* from 2 June 1936 to 13 December 1950; *Income Tax and Social Services Contributions Assessment Act 1936* from 14 December 1950 to 13 December 1965; *Income Tax Assessment Act 1936* from 14 December 1965 to 30 June 1988.

²¹ *ITAA* s 8. Current *ITAA* s 8 substituted by *Taxation Administration Act 1953*, No 1 1953.

²² See below n 26.

²³ *ITAA* s 6(1). Amended by *Income Tax (Consequential Amendments) Act 1997*, No 39 1997. *Income Tax Assessment 1997* ('*ITAA 97*') s 6-20 (definition of 'exempt income' as 'an amount of ordinary income or statutory income ... if it is made exempt from income tax by a provision of this Act or another Commonwealth law.' *Income Tax Assessment Act 1997*, No 38 1997. Date of assent 17 April 1997, commencement 1 July 1997).

the income would have been liable to tax. In *Reid v Federal Commissioner of Taxation*, Latham CJ stated:

The provisions in s 23 are very specific, applying to particular specified cases, The provision in s 23 that 'the following income shall be exempt from income tax' is a provision which presumes that, apart from the provisions contained in s 23, the income in question would fall within the other provisions of the Act making income taxable. The very object of s 23 is to exclude from taxable income which otherwise would have been taxable.²⁴

After a number of amendments to the *ITAA*, the main types of exempt superannuation funds in that Act were:

seeking exemption from income tax

- (i) funds for employees - s 23F;²⁵
- (ii) self-employed funds - s 23(ja);²⁶
- (iii) statutory and semi-government funds - s 23(jaa);²⁷
- (iv) approved deposit funds ('ADF') - s 23FA;²⁸
- (v) foreign superannuation funds - s 23(jb);²⁹ and

²⁴ *Reid v F.C. of Taxation* (1947) 8 ATD 255 257-258.

²⁵ *ITAA* s 23F provided for exemption of income, other than certain non-arm's length income, of employer sponsored funds established for the benefit of employees and their dependants.
ITAA s 23F, as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 3 1964; substituted by *Income Tax Assessment Act 1965*, No 103 1965; amended by *Income Tax Assessment Act 1973*, No 51 1973, *Income Tax Laws Amendment Act 1981*, No 108 1981, as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

²⁶ *ITAA* s 23(ja) provided exemption from income tax for the income of a provident benefit, superannuation or retirement fund established for the benefit of self-employed persons, where the number of members of the fund was not less than 20 at any time and the rules of the fund were approved by the Commissioner of Taxation as meeting published guidelines.
ITAA s 23(ja), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1952*, No 90 1952. Date of assent 18 November 1952, commencement 18 November 1952. Amended by *Income Tax Assessment Act 1965*, No 103 1965; *Income Tax Laws Amendment Act 1981*, No 108 1981, as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

²⁷ *ITAA* s 23(jaa), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, as repealed by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989.

²⁸ *ITAA* s 23FA, as inserted by No 47 1984, as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.
 Part of superannuation benefits, inter alia, payments on termination, became liable to tax effective from 1/7/83 – *ITAA* ss 27A - 27J.

(vi) life assurance company superannuation funds - s 110.³⁰

seeking tax relief when non-compliant

superannuation funds for employees and self-employed funds - s 79.³¹

It will be noted that although the policy intent was to make the concessions as broad as possible, underlying all tax concessions, including exemption, were limitations to the circumstances in which the concessions applied. Each type of fund had specific provisions to comply with in order to qualify for exemption from income tax under the *ITAA*. Except for approved deposit funds, all types of funds had the common requirement - to be established as a 'provident, benefit, superannuation or retirement fund'. The specific requirements for each of these funds to qualify for exemption from income tax under the *ITAA* are dealt with in Chapter 4 and 5.

With the introduction in 1987 of the independent legislation for the regulation of superannuation funds, the *Occupational Superannuation Standards Act 1987* ('OSSA')³² and *Occupational*

²⁹ From 1 July 1968, *ITAA* s 6(1) (definition of what constituted a 'foreign superannuation fund'). *ITAA* s 23(jb), as inserted by *Income Tax Assessment Act (No 4) 1967*, No 85 1967, effective from 1 January 1968.

³⁰ *ITAA* div 8 ss 110-116D, regulation of the taxation of superannuation funds controlled by Life Assurance Companies. Amended by *Income tax Assessment Act 1942*, No 22 1942, *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961, *Income Tax and Social Services Assessment Act (No 3) 1964*, No 110 1964, *Income Tax Assessment Act 1973*, No 51 1973, *Statute Law Reform Act 1973-1974*, No 216 1973, *Income Tax Assessment Act (No 2) 1974*, No 126 1974, *Income Tax Assessment Act 1975*, No 80 1975, *Income Tax Laws Amendment Act 1981*, No 108 1981.

³¹ *ITAA* s 79, as substituted by *Income Tax Assessment Act 1965*, No 103 1965, as amended by *Income Tax Assessment Act 1973*, No 51 1973, *Income Tax Laws Amendment Act 1981*, No 108 1981, as repealed by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984. New s 23FB funds, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

ITAA s 23FB provided for the exemption of income, other than certain non-arm's length income, of other funds that met certain rules (including a prohibition, generally, on the payment of benefits before age 55).

³² *Occupational Superannuation Standards Act 1987*, No 97 1987.

Superannuation Standards Regulations ('OSSR')³³, for the taxing provisions of superannuation funds in the *ITAA*, s 23FC³⁴ replaced:

1. s 23F³⁵ - funds established by employers for employees;
2. s 23(ja)³⁶ - self-employed funds;
3. s 23FB³⁷ - superannuation funds for employees and self-employed funds.

The definition of superannuation fund was inserted in *ITAA* to coincide with the introduction of OSSA and the transfer of the regulation of superannuation funds to the ISC. The definition of superannuation fund included:

- (a) a superannuation fund within the meaning of the *Occupational Superannuation Standards Act 1987*; and
- (b) a fund to which section 23FC applies in relation to the year of income concerned;³⁸

For the taxing provisions of ADFs in the *ITAA*, s 23FD³⁹ replaced s 23FA⁴⁰. This also coincided with the introduction of OSSA and the transfer of the regulation of ADFs to the ISC.

Where the Insurance and Superannuation Commissioner gave a notice of compliance under the OSSA to the trustee of:

1. a superannuation fund,⁴¹ *ITAA* s 23FC provided exemption of income (except for certain dividends and other non-arm's

³³ Commonwealth of Australia, *Occupational Superannuation Standards Regulations*, Statutory Rules 1987 No 322, 22 December 1987.

³⁴ *ITAA* s 23FC, as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987 first applicable to assessments for the year of income commencing 1 July 1986.

³⁵ *ITAA* s 23F, as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

³⁶ *ITAA* s 23(ja), as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

³⁷ *ITAA* s 23FB, as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

³⁸ *ITAA* s 6(1), as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987, effective 18 December 1987. See Chapter 2 [2.3].

³⁹ *ITAA* s 23FD, as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987 first applicable to assessments for the year of income commencing 1 July 1986.

⁴⁰ Under *ITAA* s 23FA, approved deposit funds that met certain requirements were exempt from tax on their investment income. The requirements related mainly to the need for the relevant fund to be established by an approved trustee to receive on deposit amounts of eligible termination payments, to deal with those amounts in accordance with specified rules and to repay the amounts with accumulated earnings at the request of the depositor. *ITAA* s 23FD, as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

length income⁴²) of that superannuation fund from income tax;⁴³ and

2. an ADF,⁴⁴ *ITAA* s 23FD provided exemption of income (except for certain dividends and excessive non-arm's length income⁴⁵) of that ADF from income tax⁴⁶.

The specific requirements for each of these funds to qualify for exemption from income tax under the *ITAA* are dealt with in Chapter 6.

The taxing and regulating provisions of *ITAA* ss 23(jaa)⁴⁷ and 23(jb)⁴⁸ remained in the *ITAA*.

Non-compliance with the provisions for exemption of income from income tax in the *ITAA* resulted in the imposition of tax on the superannuation fund at rates declared by the Parliament.⁴⁹ This reinforced the trustee's responsibility for achieving concessional tax status. In 'special circumstances', the Commissioner might have exercised his discretion and allowed a superannuation fund to be deemed complying.⁵⁰ Non-compliance might have affected the

⁴¹ *OSSA* s 12 – notices as to satisfaction of the superannuation fund conditions.

⁴² *ITAA* ss 23FC(2)-(5). *ITAA* s 23FC(6) allowed the Commissioner of Taxation to determine the extent of non-arm's length income of superannuation funds derived through any interposed partnership or trust. Because the non-arm's length income assessment provisions did not apply to s 23(ja), ss (2)-(5) only applied to income of such funds received after the date of the introduction of the *OSSA*. Chapter 3 [3.3.3] discusses the application of these exceptions.

⁴³ *ITAA* ss 23FC(1).

⁴⁴ *OSSA* s 14 – notices as to satisfaction of the approved deposit conditions of the *OSSA*.

⁴⁵ *ITAA* ss 23FD(2)-(5). *ITAA* s 23FD(6) allowed the Commissioner of Taxation to determine the extent of non-arm's length income of superannuation funds derived through any interposed partnership or trust. Chapter 3 [3.3.3] discusses the application of these exceptions.

⁴⁶ *ITAA* s 23FD(1).

⁴⁷ Statutory and semi-governmental superannuation funds.

⁴⁸ Foreign superannuation funds.

⁴⁹ *Income Tax Act 1936 to 1975* s 6; *Income Tax (Companies and Superannuation Funds) Act 1976 to 1985* s 8; *Income Tax Rates Act 1986* s 26.

⁵⁰ *ITAA* s 23F(7). See Chapter 4 [4.3.4.2].

deductibility of contributions to the superannuation fund.⁵¹

3.2.1.1 *Exceptions to exemptions*

The Federal Government introduced two exceptions to the exemptions from tax for income of superannuation funds to ensure protection of members' benefits. These were:

1. non-compliance with the 30/20 rule;⁵² and
2. dividend income derived from private companies and non-arm's length transactions, together they became known as 'special income'.⁵³

3.2.1.2 *Tax avoidance schemes*

The attitude of taxpayers has been and is to pay the least amount of tax possible.⁵⁴ Evidence of an administrative unfairness encourages individual taxpayers to start looking for ways to avoid tax.⁵⁵ Tax advisers interpret the law for taxpayers and assist them in structuring their affairs to comply with the law for the purpose of minimising their tax liability.⁵⁶ This runs contrary to the policy intent of the legislation and the response is to protect that policy position.

During the 1970s and 1980s, tax avoidance evolved into a successful industry.⁵⁷ Whatever the reasons, in the 1970s and 1980s taxpayers used artificial vehicles such as companies, partnerships, trusts and assignments of income to minimise taxation. The potential tax

⁵¹ In *FC of T v Roche* 91 ATC 5024, non-compliance with the 30/20 rule was one of the reasons cited for the income of the superannuation fund not being exempt from income tax. This, together with non-compliance with the purpose test, resulted in a deduction for contributions not being allowed under s 82AAC.

⁵² See [3.3.1].

⁵³ See [3.3.3].

⁵⁴ This attitude affirmed by decision in *IRC v Duke of Westminster* [1936] AC 1. Lord Tomlin stated: 'Every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Act is less than it otherwise would be.'

⁵⁵ Duncan Bentley, *Taxpayers' Rights: Theory, Origin and Implementation* (Kluwer Law International 2007) 49-50.

⁵⁶ Ibid 234.

⁵⁷ Ibid.

exemption of income derived by superannuation funds attracted schemes that diverted income from taxable entities to superannuation funds. Division 9C - Assessable Income Diverted under Certain Tax Avoidance⁵⁸ provided 'catch all' provisions for tax avoidance schemes. It applied to assessments in respect of income of the year of income in which 24 June 1980⁵⁹ occurred and in respect of income of all subsequent years of income.

The Division aimed at nullifying certain tax avoidance schemes that sought to exploit the tax exempt status of various bodies, organisations, associations and funds by diverting taxable income to them from individuals and companies who would otherwise have paid tax on the income. The Treasurer gave the following details of the schemes involved:

Although the details of the schemes vary, the general theme running through them is for an exempt body to acquire property from which income arises that would, but for the body's tax-exempt status, be subject to tax. The exempt bodies involved derive little benefit because they are required, in effect, to reimburse, directly or indirectly, the person from whom the income is diverted, by providing consideration in a tax-free form that is equal to most of the diverted income and which greatly exceeds the consideration that could be expected to be paid by a person not exempt from tax.

...

The thrust of the new Division is, broadly, to expose an exempt body to tax at a rate equal to the maximum personal tax rate (currently 60 per cent), on income diverted to it under a tax avoidance agreement which involves the exempt body in providing consideration – for the property giving rise to the income – which substantially exceeds what might reasonably be expected to have been provided if the body were

⁵⁸ Inserted by *Income Tax Laws Amendment Act 1981*, No 108 1981.

In summary: s 121G defines tax avoidance and the amount of diverted income which are subject to the special rate of tax; s 121H formally imposes the liability to tax and the rate of tax is declared by the *Income Tax (Diverted Income) Act 1981*; s 121F contains the interpretative provisions; s 121J provides that the ascertainment of the amount of diverted income and the tax payable thereon is an assessment for the purposes of *ITAA*; s 121K ensures that any limit imposed on the amount of Australian tax by a double taxation agreement is not affected and s 121L ensures that exempting provisions in any other federal law do not override Division 9C.

⁵⁹ The date the Treasurer announced the amendments.

to be taxed on the income at public company rates of tax (currently 46 percent).⁶⁰

Funds were specifically liable to pay tax on income diverted to them as part of a tax avoidance agreement.⁶¹ In such cases, the rate of tax imposed was the rate of tax payable by a trustee of a trust estate in pursuance of *ITAA* s 99A.⁶² In calculating the diverted income liable for tax no deductions were allowed for losses or outgoings incurred under or in connection with a tax avoidance agreement.⁶³ This protected the underlying policy position.

3.2.2 The second period – superannuation funds taxed

The second period relates to the period when superannuation funds had concessional rates of tax applied to the assessable income including taxable contributions made to the fund.⁶⁴

In 1988, the Treasurer confirmed the Federal Government's main objective in its retirement incomes policy was to ensure that all members of the population had an adequate and secure level of

⁶⁰ The Treasurer, the Hon John Winston Howard, 'Tax Avoidance Schemes' (Press Release 24 June 1980).

⁶¹ *Income Tax Assessment Act (No 6) 1980*, No 159 1980; *Income Tax (Diverted Income) Act 1981*, applicable from 24 June 1980.

⁶² *ITAA* s 121H.

⁶³ *ITAA* s 121G(8).

⁶⁴ *ITAA* div 9B, as repealed by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989, applicable to assessments for the year of income in which 1 July 1988 occurred and all subsequent years.

ITAA pt IX – 'Taxation of superannuation and related business', as inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989, amended by *Taxation Laws Amendment (Superannuation) Act 1989*, No 105 1989, as repealed by *Superannuation Legislation Amendment (Simplification) Act 2007*, No 15 2007 applicable to the 2007-2008 income year and later years.

ITAA pt IIIA, as inserted by *Income Tax Assessment (Capital Gains) Act 1986*, No 52 1986.

ITAA 97 pt 3-30 div 115 sub-div 115-A provided discount capital gains to superannuation funds, as inserted by *A New Tax System (Personal Income Tax Cuts) Act 1999*, No 69 1999.

ITAA 97 pt 3-1 s 115-100 provided for a discount of 33.33% for superannuation funds compared with other eligible entities which were allowed a discount of 50%.

ITAA 97 pt 3-30 div 295 – 'Taxation of superannuation entities', as inserted by *Tax Laws Amendment (Simplified Superannuation) Act 2007*, No 9 2007, applicable to the 2007-2008 financial year and later years.

income in retirement. He also confirmed that the second objective was to encourage 'self-provision for retirement'.⁶⁵

The Federal Government's primary objective of its tax policy of raising sufficient taxation revenue to meet the cost of public service was to keep tax rates down by spreading the burden as widely and as fairly as possible. To achieve this, new tax arrangements were to be introduced for superannuation funds. The tax concessions were to be reorganised with the ultimate tax benefits to remain unchanged.⁶⁶

With the proposed introduction of compulsory contributions by employers for their employees⁶⁷ and the access of superannuation funds to the dividend imputation system⁶⁸, the Treasurer announced the imposition of a 15% tax on fund earnings. He asserted that for most superannuation funds this would mean in practice no tax at all on investment earnings. For others, the rate would be minimal and could readily be adjusted to zero by including more Australian company shares with franked dividends in their investment portfolio. The tax was also to apply to contributions made by employers.⁶⁹ To prevent the tax concessions

⁶⁵ Commonwealth of Australia, *Parliamentary Debates*, House of Representatives, 25 May 1988, Vol H of R 161, 'Reform of the Taxation of Superannuation' forming part of the 'Economic Statement', 1 (The Treasurer the Hon P J Keating MP).

⁶⁶ Ibid.

⁶⁷ Social Security Review *Towards a National Retirement Incomes Policy* (Issues Paper No 6 Commonwealth of Australia 1988).

The *Superannuation Guarantee(Administration) Bill 1992*, the *Superannuation Guarantee Charge Bill 1992* and the *Superannuation Legislation (Consequential Amendment and Transitional Provisions) Bill 1992* referred to the Senate Select Committee. Report June 1992 with recommendations: Senate Select Committee, Parliament of the Commonwealth of Australia, *Super Guarantee Bills* (1992). *Superannuation Guarantee (Administration) Act 1992*, commenced 1 July 1992.

⁶⁸ ITAA s 160AQU(2), as inserted by *Taxation Laws Amendment (Superannuation) Act 1989*, No 105 1989, applicable in relation to dividends paid on or after 1 July 1988. Refunds were available from 1 July 2000, as inserted by *New Business Tax System (Miscellaneous) Act (No 1) 2000*, No 79 2000, replaced by ITAA 97 div 207 by *New Business Tax System (Imputation) Act 2002*, No 48 2002, effective 29 June 2002.

⁶⁹ See above n 65, 8-10 [6].

being exploited, there was to be a tightening of the maximum benefit limits.⁷⁰

It was asserted that at this time of significant growth in the superannuation industry, the proposed changes to the system of taxing superannuation funds would assist in improving the equity and efficiency of this area of the taxation system.⁷¹

From 1 July 1988, the Federal Government implemented parts of the announcement and removed the tax exemption for the income of 'complying superannuation funds'. The revenue from imposition of tax was expected to generate additional revenue of \$980 million in 1989-90 and \$1,400 million in 1990-91.⁷² The net revenue gain was expected to be smaller because of proposed reductions⁷³ in the tax payable on retirement benefits and the increase in the ceiling for deductible contributions by the self-employed and unsupported employees⁷⁴. The cost of providing the aged pension was \$9,000 million.⁷⁵

ITAA Part IX was introduced to tax superannuation funds whose income was previously exempt from tax provided they complied with the provisions of the *ITAA* that applied to them.⁷⁶ However, if the fund qualified as a complying superannuation fund within the

⁷⁰ Ibid 13-17 [8].

⁷¹ Ibid 7 [5].
Explanatory Memorandum Part A, Financial Impact, *Taxation Laws Amendment Bill (No 6) 1988*.

⁷² Ibid 10 [6].
The actual revenue received was: 1990, \$376 million; 1995, \$1,913 million; 2000, \$3,245 million; 2005, \$5,083 million; 2008, \$11,916 million. ABS Taxation Revenue 1989 to 2008.

⁷³ Ibid 13 [7].
The proposed reductions in end benefit taxes are expected to reduce lump sum tax collections by \$15 million in the 1989-90 and \$30 million 1990-91.

⁷⁴ Ibid 17 [8].
The increase in the ceiling for deductible contributions by the self-employed and unsupported employees will have a gross cost of \$40 million in 1989-90 (some of this is clawed back by the tax on contributions received by funds, allowance for which has been included in the estimates for the tax on superannuation funds.)

⁷⁵ Ibid, 1.

⁷⁶ *ITAA* pt IX, as inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989.

provisions of the OSSA, the standard component of the taxable income⁷⁷ continued to receive concessional tax treatment.⁷⁸ An amended definition of superannuation fund to align with the introduction of Part IX included an ‘eligible superannuation fund within the meaning of Part IX’⁷⁹. An ‘eligible superannuation fund’, in relation to a year of income, meant ‘a fund that was a complying superannuation fund, or a non-complying superannuation fund, in relation to the year of income.’⁸⁰ Complying superannuation funds were those that satisfied standards set down in the OSSA. A ‘complying superannuation fund’, in relation to a year of income, was a fund in respect of which:

- (a) the Insurance and Superannuation Commissioner has given a notice under section 12 of the OSS Act stating that the Insurance and Superannuation Commissioner is satisfied that the fund satisfied the superannuation fund conditions in relation to the year of income; or
- (b) the Insurance and Superannuation Commissioner has given a notice under section 13 of the OSS Act stating that the Insurance and Superannuation Commissioner is satisfied that the fund should be treated as if it has satisfied the superannuation fund conditions in relation to the year of income.⁸¹

The new taxation arrangements introduced by the 1989 legislation⁸² applied to the following classes of complying funds:

- superannuation funds established by employers to provide benefits for their employees and dependants;

⁷⁷ ITAA s 285 defined the standard component of taxable income as the amount (if any) remaining after deducting the special component from the taxable income. ITAA s 284 defined the ‘special component’ of the taxable income remaining (if any) after deduction from the special income:

- (a) any allowable deductions that relate exclusively to the special income; and
- (b) so much of any other allowable deduction as, in the opinion of the Commissioner, may appropriately be related to the special income.

See below n 196].

⁷⁸ ITAA pt IX div 3 s 278; *Income Tax Rates Act 1986* s 26.

⁷⁹ ITAA s 6(1), substituted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989, effective 30 June 1989.

⁸⁰ ITAA s 267(1).

⁸¹ Ibid.

⁸² See above n 64.

- personal superannuation funds, often used by self employed persons and employees who do not receive employer superannuation support;
- public sector superannuation funds generally⁸³;
- approved deposit funds; and
- pooled superannuation trusts ('PST')⁸⁴ which were established as investment vehicles for complying superannuation and approved deposit funds.⁸⁵

In addition to the imposition of tax on their income, superannuation funds were to be taxed on certain contributions and amounts rolled over to a fund. These taxable contributions were included in a superannuation fund's assessable income. They included:

- all contributions made to a superannuation fund by an employer on behalf of employees;⁸⁶
- contributions made to a personal superannuation fund by a fund member, to the extent that the contributions were deductible to the member;⁸⁷ and
- the post-30 June 1983 components of rolled-over eligible termination payments paid by employers, e.g. golden handshakes, and any eligible termination payments sourced in a fund and held not taxable under the new arrangements.⁸⁸

Other features included:

- where a superannuation fund paid benefits in the form of pensions, part of the investment earnings of the

⁸³ To avoid any possibility of infringement of *Constitution* s 114, which prohibits the Commonwealth from imposing tax on any State, the law contained a safeguard to prevent the application of the new provisions if they had that effect.

⁸⁴ *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989.

⁸⁵ See Chapter 6 [6.3].

⁸⁶ *ITAA* s 274.

⁸⁷ *Ibid.*

⁸⁸ *ITAA* s 27D.

superannuation fund remained exempt. The exemption applied to the proportion of a superannuation fund's income that its current pension liabilities bore to its total liabilities;⁸⁹

- superannuation funds received full imputation rebates notwithstanding that part of the fund's franked dividend income could be exempt because the fund had current pension liabilities;⁹⁰
- the cost to a complying superannuation fund of providing death and disability benefits was to be deductible to the fund in order to allow funds to continue to provide after tax benefits at the same level as before the introduction of the tax on superannuation contributions.⁹¹

In 1994, the definition of superannuation fund was substituted in the *ITAA* to align with the introduction of the *SISA*.

Superannuation fund means:

- (a) a scheme for the payment of superannuation benefits upon retirement or death; or
- (b) a superannuation fund within the definition of 'superannuation fund' in section 10 of the *Superannuation Industry (Supervision) Act 1993*.⁹²

To be eligible for concessional tax treatment a superannuation fund had to be a 'complying superannuation fund'. The definition of a 'complying superannuation fund' was amended in the *ITAA* to align with the introduction of the *SISA*.

A superannuation fund was a complying superannuation fund and qualified for concessional tax treatment under the *ITAA* if:

1. the prudential Regulator had given a notice to the fund that it was a complying superannuation fund in relation to a year

⁸⁹ *ITAA* s 282B.

⁹⁰ *ITAA* s 160AQU(2).

⁹¹ *ITAA* s 279.

⁹² *ITAA* s 6(1), substituted by *Taxation Laws Amendment Act (No 4) 1994*, No 181 1994.

- of income and had not subsequently given a notice to the fund that it was not a complying superannuation fund;⁹³ and
2. the superannuation fund
 - (i) was a resident regulated superannuation fund at all times during the year of income when it was in existence; and
 - (ii) (a) the trustee did not contravene the *SISA* or *SISR* in relation to the fund in respect of the year of income; or
 - (b) the trustee contravened the *SISA* or *SISR* in respect of the year of income on one or more occasions but the fund did not fail the culpability test⁹⁴ in relation to any of those contraventions.⁹⁵

A non-complying superannuation fund could be a fund which –

- did not come within the definition of a superannuation fund in the *OSSA/SISA*; or
- failed to meet one or more of the standards or conditions imposed under that Act and the Regulations.

No deduction was allowed for premiums paid in respect of insurance of death and disability benefits⁹⁶. No provision was made for the transfer of taxable contributions from a non-complying fund to a life office or a pooled superannuation trust⁹⁷.

From 1 July 2007, the taxation law applicable to superannuation funds was rewritten from the *ITAA* into *ITAA 97*⁹⁸ as part of the

⁹³ *SISA* s 45.

⁹⁴ *SISA* ss 40, 41.

⁹⁵ *SISA* s 42(1).

⁹⁶ *ITAA* s 279 applied only to complying superannuation funds, as inserted by *Taxation Laws Amendment (Tax File Numbers) Act 1988*, No 97 1989 applicable to assessments for the year of income in which 1 July 1988 occurred and all subsequent years.

⁹⁷ *ITAA* s 275 applied only to complying superannuation funds, as inserted by *Taxation Laws Amendment (Tax File Numbers) Act 1988*, No 97 1989 applicable to assessments for the year of income in which 1 July 1988 occurred and all subsequent years.

⁹⁸ *ITAA 97* pt 3.30. *ITAA 97* div 295 applied to the taxation of superannuation entities.

reforms designed to streamline and simplify the complex tax arrangements that had evolved over the years, improve the incentives to save, increase retirement income and strengthen incentives for older Australians to stay in the workforce.⁹⁹ As part of the Federal Government's initiative to simplify superannuation, Part IX of *ITAA* was repealed¹⁰⁰ and replaced by Part 3-30 Superannuation in *ITAA* 97.¹⁰¹

Non-compliance with the provisions for concessional treatment of income resulted in the imposition of tax on the superannuation fund at rates declared by the Parliament.¹⁰²

The effect of the Federal Government's strategy was measured by the changes in the numbers of the workforce that had superannuation and the amount invested in superannuation funds. Initially, incentives were in the form of tax incentives. This was successful in that there was an increase in those in the workforce that had superannuation from 32% in 1974¹⁰³ to 55% of employees aged 15 to 64.¹⁰⁴ The assets of superannuation funds increased from \$32 billion in 1983¹⁰⁵ to \$119 billion in 1989.¹⁰⁶

The imposition of income tax on superannuation funds in 1988 not only protected the source of income of the Federal Government but also enabled the continued concessional tax treatment of superannuation funds. Coupled with the increase in the number of

⁹⁹ See above n 16.

¹⁰⁰ *ITAA* pt IX, as repealed by *Tax Laws Amendment (Simplified Superannuation) Act* 2007, No 9 2007. *ITAA* div 295, as inserted by *Tax Laws Amendment (Simplified Superannuation) Act* 2007, No 9 2007 applicable to the 2007-2008 income year and later years.

¹⁰¹ *Tax Laws Amendment (Simplified Superannuation) Act* 2007, No 9 2007.

¹⁰² *Income Tax Rates Act* 1986 s 26.

¹⁰³ Leslie Nielson, Economic Section, Parliament of Australia, 'Chronology of superannuation and retirement income in Australia', (Parliamentary Library, Commonwealth of Australia, 1900-2010).

¹⁰⁴ ABS Superannuation, Australia, 6319.0, 1988.

¹⁰⁵ The Treasurer, the Hon John Kerin MP, 'Prudential Supervision of the Superannuation Industry' (Press Release, No 73, 20 August 1991).

¹⁰⁶ ISC Annual Report 1989-90.

superannuation funds available to contribute to and the introduction of compulsory contributions, the concessional treatment of the income of superannuation funds did encourage people to save for their own retirement. The assets of superannuation funds increased further to \$148 billion in 1992.¹⁰⁷ With the introduction of compulsory contributions, coverage had increased to 91% of the workforce in 2000¹⁰⁸ and superannuation assets rose to \$484.2 billion by 2000.¹⁰⁹

3.2.2.1 Contribution surcharge

From 20 August 1996,¹¹⁰ a superannuation contributions surcharge was imposed¹¹¹ on members' surchargeable contributions¹¹² made on behalf of taxpayers whose income for the year exceeded the surcharge threshold.¹¹³ The surcharge was only applied if the adjusted taxable income of the member was above the surcharge threshold for the year, the intention being that only high income earners were affected. The rate of the surcharge depended on the adjusted taxable income of the member.¹¹⁴ The person liable to pay varied according to who had the capacity to pay. In the first instance, the trustee would receive the assessment. If the trustee did not have member benefits to make the payment from, the ATO assessed the member.¹¹⁵

¹⁰⁷ ISC Annual Report 1991-92.

¹⁰⁸ ABS, '2000 Survey of Employment Arrangements and Superannuation', Superannuation, Australia',

¹⁰⁹ APRA, 'Insight 2007, Superannuation Coverage and Financial Characteristics' ABS Catalogue 6360.0.

¹¹⁰ *Surcharge Contributions Tax Imposition Act 1997*, No 187 1997 ('SCT').

¹¹¹ SCT s 4.

¹¹² *Superannuation Contributions Tax (Assessment and Collection) Act 1997*, No 70 1997 ('SCTACA'); *Superannuation Contributions Tax (Assessment and Collection) Regulations 1997*, Statutory Rules 1997 No 271, *Gazette*, 24 September 1997.

¹¹³ SCTACA s 9.

¹¹⁴ SCT ss 5-7. The maximum surcharge rate was defined in SCT s 5(1AA). The maximum surcharge rate before 2003/04, 15%; 2003/04, 14.3%; 2004/05, 12.5%.

¹¹⁵ SCTACA s 10.

The surcharge was introduced in 1996 when the budget was deeply in deficit. When this measure was no longer required to keep the budget in balance in 2005, the superannuation contributions surcharge was not payable on contributions made on or after 2005. Approximately 600,000 were estimated to receive a boost to their superannuation savings as a result of this measure.¹¹⁶

3.3 Additional requirements for exemption/tax concession

For a superannuation fund to qualify for exemption or tax concessional treatment, additional requirements had to be met. These additional requirements provided benefits for the Federal Government and members of superannuation funds. The 30/20 rule provided capital to the Federal Government. The 'special income' rules protected the Revenue. The 'in-house asset rules' protected the benefits of members by restricting investment of superannuation funds' assets. Non-compliance with these rules could result in either withdrawal of the exemption status or the imposition of a non-concessional tax rate on the superannuation fund. This in turn affected the members' benefits.

3.3.1 30/20 rule

In 1961, a qualification to the exemption was introduced because of the Commonwealth and State Governments' difficulties in financing their works programs.¹¹⁷ There was reduced support for public authority loans by the life companies¹¹⁸ and the privately

¹¹⁶ The Treasurer, the Hon Peter Costello MP, 'Superannuation Laws Amendment (Abolition of Surcharge) Bill 2005' (Second Reading Speech at the House of Representatives, Canberra, 2005).

¹¹⁷ The Treasurer, the Rt Hon Harold Holt MP 'Income Tax and Social Services Contribution Assessment Bill 1961' (Second Reading Speech at the House of Representatives, Canberra).

¹¹⁸ Ibid. Life companies held 50% of assets in public authority securities in 1939, 68% in 1949, 37% in 1959 with an estimated 33% in 1960. Ibid 2nd reading speech.

managed superannuation and provident funds.¹¹⁹ To counter this reduction in support for public authority loans, new taxation arrangements for privately managed superannuation and provident funds were inserted into *ITAA*.¹²⁰

The initial requirements in *ITAA*¹²¹ required compliance by two categories of superannuation funds. These categories were superannuation funds established for employees by employers and superannuation funds for self-employed persons. Public sector plans were excluded from the requirement to comply with the 30/20 rule by the definition of superannuation fund.¹²²

If privately managed funds complied with *ITAA* ss 23(j) or (ja) and were established after 1 March 1961, their income would be fully exempt from taxation provided they maintained in their investment portfolios public authority securities¹²³ which cost at least 30% of

¹¹⁹ Larger privately-managed superannuation funds held 50% of assets in public authorities securities in 1956, which dropped to 39% in 1959.

¹²⁰ Division 9B - Superannuation Funds, ss 121B - 121E, as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 of 1961. The '30/20 rule' was included in this Division in ss 121C(1)-(12), effective from 1 March 1961. The validity of the insertion of Division 9B was challenged in *Fairfax v FC of T* [1965] 14 ATD 135 as being a law not with respect to taxation but promoting investment in public securities. It was held that the enactment was valid.

¹²¹ *ITAA* ss 121(1)-(12), as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961.

¹²² *ITAA* s 121B, definition of 'superannuation fund', as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961.

¹²³ *ITAA* s 6(1) (definition of 'public securities' to mean:

- (a) Commonwealth securities;
 - (b) bonds, debentures, stock or other securities issued by a State, Territory, municipal corporation, local governing body or public authority set up under a Commonwealth, State or Territory law;
 - (c) securities issued in respect of a loan to a company whose principal business is the supply and distribution in the Commonwealth of gas, water or electricity by a system of reticulation
- but did not include:
- (d) securities referred to in paragraph (b) (not being securities to which paragraph (e) applies) issued in respect of a loan raised outside Australia and the Territories unless there is in force a declaration by the Treasurer, published in the Gazette that those securities shall be public securities for the purposes of this Act; or
 - (e) securities issued after 12 April 1976 by a bank).

Inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961.

all the assets of the fund. At least 20 % of this 30% invested in public authority securities had to be invested in Commonwealth securities.¹²⁴

For privately managed funds that were established before 1 March 1961, different rules for the assessment of the assets applied.¹²⁵

From 1964, *ITAA* ss 23F and 23(jaa) replaced *ITAA* s 23(j)(i).¹²⁶ With this substitution, the definition of ‘superannuation fund’ to which the 30/20 rule applied excluded superannuation funds established for the public sector.¹²⁷ This exclusion continued until the abolition of the rule on 30 June 1984.¹²⁸

The 30/20 rule applied to life assurance companies generally.¹²⁹ This application of the rule, by definition, extended to the superannuation business of the life assurance companies.¹³⁰ There was specific exclusion for non-resident superannuation funds from complying with the 30/20 rule.¹³¹

The Commissioner could disregard any failure to comply with the 30/20 rule at all times during the year of income if he considered that:

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- ¹²⁴ In *Case L55 79* ATC 404 determined that money deposited with a State authority under an extension agreement was not a ‘debenture’ as defined by *ITAA* s 6(1) nor was it ‘issued’ as required by *ITAA* s 6(1).
¹²⁴ *ITAA* s 121C(1).
 In *Case W100 89* ATC 813, the AAT addressed what was the ‘cost of assets’ and it stated that it was the cost of the beneficial interest. The application of the 30/20 rule was not a deciding factor in this case.
- ¹²⁵ *ITAA* ss 121C(2), (3).
- ¹²⁶ *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. This Act amended s 121C to reflect the changes in s 23 relating to superannuation funds.
- ¹²⁷ By identifying the types of superannuation funds to which s 121C applied in s 121C(1A) as *ITAA* ss 23(ja) and 23F, public sector funds in *ITAA* s 23(jaa) were excluded. *ITAA* s 121C(1A), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964.
- ¹²⁸ Repealed by *Taxation Laws Amendment Act 1985*, No 49 1985.
- ¹²⁹ *ITAA* s 110A.
- ¹³⁰ *ITAA* ss 110, 112A.
- ¹³¹ *ITAA* s 121C(6).

- the trustee of the fund had made a bona fide and genuine attempt to maintain the prescribed proportion of public securities;¹³² or
- the failure to do so was the result of a temporary delay in investing the moneys of the fund;¹³³ and
- upon application by the trustee of the fund, that compliance would endanger the fund's stability and would be unreasonable in the circumstances.¹³⁴

Including statutory rules dictating minimum levels of investment in 'public securities' limited the level of investment by a superannuation fund established by the employer for its employees in that employer and by self-employed persons in their businesses.¹³⁵

The consequence of non-compliance with the 30/20 rule on investment of assets was the imposition of tax at rates declared by the Parliament¹³⁶ on 'investment income'¹³⁷. If the investment

¹³² ITAA s 121C(4)(a).

The Commissioner exercised his discretion to disregard failure to comply with the 30/20 rule: *Case K8 78 ATC 87*.

The Commissioner did not exercise his discretion to disregard failure to comply with the 30/20 rule: *Case T53 86 ATC 416*; *Case U23 87 ATC 190*; *Case U167 87 ATC 959*.

¹³³ ITAA s 121C(4)(b). *Case U139 87 ATC 803*; *Case T70 86 ATC 1029*; *Case U167 87 ATC 959*.

¹³⁴ ITAA s 121C(5). In *Case QT85/667 and the Commissioner of Taxation and QT85/1074 and Commissioner of Taxation*, it was decided that s 121C(5) was not an issue and there was no evidence before the Tribunal suggesting that the Fund's financial stability was in danger.

¹³⁵ ITAA ss 23(j), 23(ja).

¹³⁶ For ITAA ss 23F, 23(ja) superannuation funds, ITAA s 121D.

ITAA s 121D, as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961, as repealed by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, substituted s 121D within inserted ss 121CA-121DE to apply in relation to assessments on income of the 1965-1966 income year.

Rates applied: *Income Tax Act 1936 to 1975* s 6(5); *Income Tax (Companies and Superannuation Funds) Act 1976 to 1985* s 8(2).

For superannuation fund established by life assurance companies, *Income Tax Act 1936 to 1975*; *Income Tax (Companies and Superannuation Funds) Act 1976-1985*; *Income Tax Rates Act 1986*.

¹³⁷ The original definition of investment income in relation to a superannuation fund included in s 121B, as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961 meant:

income of a superannuation fund was subject to tax, a rebate was allowed for Commonwealth interest included in the investment of the superannuation fund. A rebate was not available for dividends and a superannuation fund was not liable to pay provisional tax except on income assessed for non-compliance.¹³⁸

The provisions of s 121C requiring compliance with the 30/20 rule were abolished on 11 September 1984¹³⁹ with effect from the commencement of that year of income. Its abolition had been considered by different Committees appointed by the Federal Government¹⁴⁰ but its abolition was part of the Government's process of deregulating Australia's financial system. Its abolition was not expected to have any discernible effect on the revenue.¹⁴¹

the income of the fund that, but for paragraph (j) or (ja) of section twenty-three of this Act, would be assessable income, other than contributions to the fund, calculated as if the trustee of the fund were a taxpayer in respect of that income, being a resident, less all amounts that would be allowable deductions (other than the concessional deductions, deductions in respect of benefits and deductions under section seventy-nine of this Act) if that income were assessable income;

The original definition was repealed and replaced by a new definition by *Income Tax and Social Services Contribution Assessment Act 1964*, (No 3) 1964 to reflect the amended regulating provisions in relation to superannuation funds established by employers for the benefit of their employees and their dependants.

¹³⁸ ITAA s 121DD, as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961, as repealed by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 of 1964. Substituted ITAA s 121DD, as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, amended by *Income Tax Assessment Act 1965*, No 103 1965, *Income Tax Assessment Act (No 3) 1972*, No 47 1972, *Income Tax Assessment Amendment Act (No 3) 1977*, No 126 1977.

¹³⁹ Repealed by *Taxation Laws Amendment Act 1985*, No 49 1985.

¹⁴⁰ The Asprey Committee (see above n 10) suggested that the 30/20 Rule should be reconsidered. If it was to be retained, the issue of a special index-linked bond should be considered. Also, there should be a market at all times for any security that a superannuation fund was required to hold [21-107].

The Hancock Committee (See above n 10) referred to this recommendation in their Final Report but did not adopt any view on the desirability of retaining the 30/20 provision but objected to the selected application of the 30/20 rule 119-120 [7.59].

¹⁴¹ The Treasurer, the Hon PJ Keating MP 'Taxation Laws Amendment Bill 1985' (Second Reading Speech at the House of Representatives, Canberra).
The Campbell Report (See above n 10) recommended that the Federal Government should abolish the 30/20 requirement and rely on market-directed initiatives to appropriately fund its borrowings 181 [10.38]. It recommended that there should not be a transition period 182 [10.44].

3.3.2 *In-house asset rules*

The decision to implement the in-house asset rules¹⁴² commencing on 1 July 1985¹⁴³ reflected the Government's concern that excessive investment by a superannuation fund in the sponsoring employer's business may mean, in the event of the failure of that business, that employees lose not only their jobs, but also their superannuation entitlements.¹⁴⁴ These limits on the tax concessions were directly related to protection of members' assets, the original policy intent behind the establishment of superannuation funds. It was stated that the introduction of the in-house asset rules for employer-sponsored superannuation funds should have no effect on the Government's revenue.¹⁴⁵

The Federal Government introduced the 'in-house asset rules' to limit the proportion of the fund's assets that could be lent to or invested in the sponsoring employer or an associate of such an employer.

The in-house rules applied:

- from 1 July 1985 to the introduction of the OSSA and OSSR;¹⁴⁶
- with the introduction of the regulation by the OSSA¹⁴⁷ and OSSR;¹⁴⁸ and subsequently;

¹⁴² ITAA s 121C, substituted by *Taxation Laws Amendment Act (No 2) 1985*, No 123 1985.

¹⁴³ Technically, this meant that most funds would qualify for exemption from tax on their investment income without having to satisfy the 30/20 rule at any time during 1984/85. However, Taxation Ruling IT 2275 [4] advised that s 23F funds, for 1984-85 income year, were not to lend back to the employer sponsor of the fund (either directly or indirectly) a larger amount than would have been permitted had the 30/20 rule continued to apply. If a s 23F fund lent more than 70% of the gross cost of the fund's assets to the employer sponsor, the income of the fund for that year of income could be taxed in terms of ITAA s 121DAB.

¹⁴⁴ See above n 10.

¹⁴⁵ The Minister Assisting the Treasurer the Hon Chris Hurford MP, 'Taxation Laws Amendment Bill (No 2) 1985' (Second Reading Speech at the House of Representatives, Canberra).

¹⁴⁶ 1 July 1985 to 30 June 1986. ITAA ss 121C, 121CC, as inserted by *Taxation Laws Amendment Act (No 2) 1985*, No 123 1985, first applicable to assessments for the year of income commencing 1 July 1985, as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

- with the introduction of *SISA* and *SISR* up to the current time.¹⁴⁹

Initially, the *OSSR*¹⁵⁰ referred the application of the in-house asset rules to relevant provisions of the *ITAA*.¹⁵¹

From 1 July 1990, similar provisions in the *ITAA* for the application of the in-house asset rule were incorporated into the *OSSR* with reference to the *ITAA* omitted¹⁵². With the exception of imposing the in-house asset restrictions on public sector funds¹⁵³

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- ¹⁴⁷ From 1 July 1986 to 30 June 1994.
ITAA s 23FC for superannuation funds, replaced s 23FB, as inserted by *Taxation Laws Act (No 4) 1987*, No 138 1987 first applicable to assessments for year of income commencing 1 July 1986.
ITAA s 23FD for approved deposit funds, replaced s 23FA, as inserted by *Taxation Laws Act (No 4) 1987*, No 138 1987 first applicable to assessments for year of income commencing 1 July 1986. The amount on which the trustee of a superannuation fund or an approved deposit fund was assessable and liable to pay tax under the provisions of Division 9B was deemed to be the taxable income of the fund by former s 121DC. Substituted by *Taxation Laws Act (No 4) 1987*, No 138 1987 effective for the 1986/87 and subsequent years of income. *ITAA* s 121DAAA imposed tax on special income received by an approved deposit fund.
- ¹⁴⁸ From 1 July 1986 to 1993. Initially *OSSR* reg 16 – Investment Standards, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations*, Statutory Rules 1987 No 322 1987, 22 December 1987. The commencement date of the Regulation varied depending on the regulation, with the first date being 1 July 1986. See below n 151.
- ¹⁴⁹ From 1993, as inserted by *Superannuation Industry (Supervision) Consequential Amendments Act 1993*, No 82 1993 applicable in relation to a fund for the 1994/1995 year of income of the fund and for all later years of income.
- ¹⁵⁰ *OSSR* reg 16(4).
- ¹⁵¹ *ITAA* ss 121C(4), (5), (6), as inserted by *Taxation Laws Amendment Act (No 2) 1985* No 123 1985 first applicable to assessments for the year of income commencing 1 July 1985. The paragraphs on In-house Asset Rules in *Income Tax Ruling IT 2293* were superseded by [34]-[62] of the ISC Circular No 18.
- ¹⁵² *OSSR* reg 16A Investment standards: in-house assets, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 185, 29 June 1990, commenced on 1 July 1990.
OSSR reg 16B – Prohibition on new in-house asset acquisitions, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)* No 14 1993, 29 January 1993, commencement date 29 January 1993.
- ¹⁵³ *OSSR* reg 16A(1), the definition of in-house asset does not include investment in government securities by a public sector fund.

and life assurance companies¹⁵⁴, no substantive changes were made to the new regulation.¹⁵⁵

The basic rule required that at all times during the income year the cost of the ‘in-house assets’ of an employer-sponsored superannuation fund should not exceed 10% of the cost of all the assets of the fund.¹⁵⁶ In-house assets of a fund were those assets that consisted of loans to or investments¹⁵⁷ in an employer-sponsor¹⁵⁸ or an associate¹⁵⁹ of an employer-sponsor. The application of the rules varied according to whether the fund was established before 12 March 1985 or on or after that date.¹⁶⁰

¹⁵⁴ Ibid. The definition of in-house asset does not include a life insurance policy on a member where the employer sponsor is a life assurance company.

¹⁵⁵ ISC Circular No 18 [30].

¹⁵⁶ *ITAA* s 121C(18) provided for funds that commenced or ceased during the year. The rules only applied for that part of the year the fund was in existence.

¹⁵⁷ *ITAA* s 121C(1) defined ‘investment’ as any mode of application of money for the purpose of gaining interest, income or profit.

¹⁵⁸ An employer who contributed to a superannuation fund for the benefit of an employee (including a director) or dependants of an employee was treated as an employer-sponsor of the fund – *ITAA* s 121C(2)(a). A company controlled by the employer and which contributed to the fund was also treated as an employer-sponsor – s 121(2)(b).

Where the employer was a company, any person connected with the employer company and who contributed was deemed to be connected with a corporate employer where:

- the person has a controlling interest in the employer;
- the person was a company in which the controlling interest was held by a person who had a controlling interest in the employer; or
- the person was the beneficial owner of shares in the employer – s 121C(3).

¹⁵⁹ *ITAA* s 121C(1) referred to *ITAA* s 26AAB for the definition of ‘associate’. In broad terms, any person who, by reason of business or family connections, was regarded as being associated with a particular person – s 26AAB(14). Case: *Trevisan (Trustee of Forli Pty Ltd Superannuation Fund v FC of T* 91 ATC 4416 (appeal against decision of the AAT reported as *Case X70*, 90 ATC 537) – decision that units in employer-sponsor’s property trust were not by definition in-house assets.

¹⁶⁰ For funds established after 11 March 1985, the basic 10% rule first applied for the 1985/86 year of income. The restriction should have been complied with at all times during the income year – s 121C(4).

For funds established before 12 March 1985, *ITAA* s 121C(5) provided that the 10% limit was phased-in over a 10 year period so that the funds could meet the limit by natural growth rather than by mandatory repayment of loan-backs to the employer sponsor. The rule for these funds over the phasing-in period from 1 July 1985 to 30 June 1995 was that the cost of the fund’s in-house assets must not exceed at any time during the relevant income year the greater of:

- the cost of the in-house assets held as at 11 March 1985 but must not exceed 70% of the cost of all assets of the fund at that date; and
- 10% of the cost of all the assets of the fund – s 121C(5)(a), (6).

The concessional treatment of funds existing on 11 March 1985 continued until the end of the income year commencing 1 July 1994. For the year commencing 1 July 1995 and later

For the application of the in-house asset rules for the regulation of superannuation funds by the *OSSA* and *OSSR*, see Chapter 6.

For the application of the in-house asset rules for the regulation of superannuation funds during the period of the *SISA* and *SISR*, see Chapter 7.

The consequence of non-compliance with the in-house asset rules was that the investment income of the fund was taxed at the rate of the imposition of tax declared by the Parliament.¹⁶¹ The employer and employee contributions were not deductible for income tax purposes.¹⁶²

3.3.3 ‘Special Income’

Shortly after the introduction of the 30/20 rule, the Ligertwood Committee in a report to the Federal Government of its investigations into tax avoidance¹⁶³ recommended that new provisions authorise exemption of the income of superannuation funds if the Commissioner was satisfied that certain tests were met. In addition, it recommended that the exemption of income of any superannuation fund should not extend to dividends and, in certain circumstances, other income derived from arrangements made with a private company. Also to be taxed in full, irrespective of any exemption otherwise available, was income from a transaction by a superannuation fund with a person with whom the fund was not dealing at arm’s length.¹⁶⁴

years, the 10% limit was applied to all funds regardless of when they were established - ss 121C(4), (5)(b).

ITAA s 121C substituted by No 138 1986, first applicable to assessments for the year commencing 1 July 1986, as repealed by No 138 1987.

¹⁶¹ ITAA s 121CC from 1 July 1985. Rates applied: *Income Tax (Companies, Corporate Unit Trusts and Superannuation Funds) Act 1985* s 8(2); *Income Tax Rates Act 1986* s 26.

¹⁶² ITAA s 82AAC(2). *Taxation Appeals [1993]* AATA 389.

¹⁶³ Commonwealth Committee on Taxation, Commonwealth Government of Australia, *Report of the Commonwealth Committee on Taxation* (1961).

¹⁶⁴ Ibid 155-7.

These amendments proposed by the Ligertwood Committee directly protected the Federal Government's Revenue by preventing the diversion of income to a lower taxed entity and transactions on a non-arm's length basis.¹⁶⁵ Assessing private company dividends received by superannuation funds as taxable also ensured that the holding of shares by a superannuation fund was not designed to provide a means of siphoning off tax free dividends for the benefit of members as shareholders.¹⁶⁶

The Federal Government considered that a blanket withdrawal of the exemption relating to dividends from private companies as recommended by the Ligertwood Committee was too severe. It proposed instead that each individual case be examined on its merits by the Commissioner of Taxation to determine whether such dividends should be taxed in full in the hands of the trustee of the superannuation fund, irrespective of any exemption available.¹⁶⁷ The Federal Government adopted the recommendations of the Committee relating to the taxation of dividends received from private companies subject to the Commissioner's opinion as to reasonableness for exemption.¹⁶⁸

These rules relating to the dividends from private companies and non-arm's length transactions applied from 23 November 1964.¹⁶⁹ They were replaced unchanged except for consequential references as part of the substitution of ITAA s 23F in 1965.¹⁷⁰ The

¹⁶⁵ *Case A39*, 69 ATC 227, *Case A40*, 69 ATC 229, *Case B40*, 70 ATC 202.

¹⁶⁶ *Case E56* 73 ATC 442.

¹⁶⁷ The Treasurer, RG Casey, 'Income Tax and Social Services Contribution Assessment Bill (No 3) 1964' (Second Reading Speech at the House of Representatives, Canberra).

¹⁶⁸ *Income tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, date of assent and commencement 23 November 1964.

¹⁶⁹ Inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, Date of Royal Assent, commencement 23 November 1964.

¹⁷⁰ ITAA ss 23F(8), (9), (10), replaced by ss 23F(14), (15), (16) by *Income Tax Assessment Act 1965* No 103 1965.

introduction of s 23FB¹⁷¹ (funds for gainfully occupied persons) and approved deposit funds¹⁷² in 1984 included the same provisions as in s 23F relating to the tax consequences of private company dividends and non-arm's length income.¹⁷³ They continued until the introduction of the OSA on 1 July 1986.¹⁷⁴ In 1988, the introduction of *ITAA* Part IX (the taxation of superannuation funds), these types of income became known collectively as 'Special Income'.¹⁷⁵ The taxation provisions from *ITAA* Part IX¹⁷⁶ were transferred to Part 3-30 of the *Income Tax Assessment Act 1997* in 2007.¹⁷⁷ The term 'special income' was replaced by 'non-arm's length income'.¹⁷⁸

A dividend paid to a superannuation fund by a private company was not exempt from income tax unless the Commissioner was of the opinion that it would be reasonable to exempt the dividend having regard to:

- (a) the paid-up value of the shares in that company that are assets of the fund;
- (b) the cost to the fund of the shares on which the dividend was paid by the company;

¹⁷¹ Inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984 applicable to assessments for the year of income commencing 1 July 1984 and all subsequent years.

¹⁷² *ITAA* s 23FA, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984 applicable to assessments for the year of income commencing 1 July 1984 and all subsequent years.

¹⁷³ *ITAA* s 23FB(13)-(15).
ITAA s 121CB imposed tax on income of s 23FB superannuation fund that comprised (1) private company dividends for which the Commissioner has not exercised his discretion under *ITAA* s 23FB(13) to exempt the dividends from tax; and (b) other income not exempt from tax by reason of s 23FB(15) being income derived from a transaction where the parties to the transaction were not dealing at arm's length with each other in relation to the transaction and where the income was greater than might have been expected had the parties been so dealing at arm's length.
 Income on which a trustee was assessable and liable to pay tax under *ITAA* s 121CB was deemed to be taxable income of the fund concerned in *ITAA* s 121DC. Rates in *Income Tax Rates Act 1986*.

¹⁷⁴ Repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

¹⁷⁵ *ITAA* s 273, as inserted by *Taxation Laws Amendment Act (No 2) of 1989*, No 97 1989.

¹⁷⁶ Repealed by *Superannuation Legislation Amendment (Simplification) Act 2007*, No 15 2007 applicable to the 2007-2008 income year and later years.

¹⁷⁷ Inserted by *Tax Laws Amendment (Simplified Superannuation) Act 2007*, No 9 2007 applicable to the 2007-2008 income year and later years.

¹⁷⁸ *ITAA* 97 s 295-550, as inserted by No 9 2007 applicable to the 2007-2008 income year and later years.

- (c) the rate of the dividend paid to the fund by the company on the shares in the company that are assets of the fund;
- (d) whether the company has paid a dividend on other shares in the company and, if so, the rate of that dividend;
- (e) whether any shares have been issued by the company to the fund in satisfaction of, or of a part of, a dividend paid by the company, and, if so, the circumstances of the issue of those shares; and
- (f) any other matters that the Commissioner considered relevant.¹⁷⁹

The acquisition of private company shares by a superannuation fund at less than full value was a factor that resulted in the dividends not being included in the exempt income of a superannuation fund.¹⁸⁰ This was especially relevant when shares were issued to a superannuation fund at less than their value where other shareholders were involved and by the transaction were disadvantaged.¹⁸¹ When the rate of dividend paid by the private company was equal for all holders of shares, the Commissioner could accept that it was reasonable to exempt the dividend from tax. This was not a determining factor when other factors dominated the argument in favour of the Commissioner.¹⁸² Circumstances of a transaction by a superannuation fund and its investment in and relationship with a private company could be

¹⁷⁹ ITAA s 23F(8), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. ITAA s 23F(16) as part of the s 23F substituted by *Income Tax Assessment Act 1965*, No 103 1965.

¹⁸⁰ ITAA s 23F(a), (b). *Case A39*, 69 ATC 227, *Case A40*, 69 ATC 229. Whether paragraphs (a) and (b) of s 23F(16) should be read together, as was the case in these two cases, was challenged before the Board in *Case B40*, 70 ATC 202. These paragraphs had to be read together to interpret 'value' of the shares. It was considered by the Board that even if this was correct which was not conceded, paragraph (f) 'any other matters the Commissioner thinks relevant' would include the value of the shares as relevant to deciding the Commissioner's position.

Case A38 69 ATC 225 involved a non-contributory fund – s 23F(16)(b) (the acquisition of the shares at less than full value), s 23F(16)(f) (any other matters the Commissioner thinks relevant). In this case, in addition to the fund acquiring the shares at less than full value, the fact that the employer was the sole contributor to the superannuation fund and that the fund was entitled to one-fifth of all distributed profit were relied on by the Board in making their decision to confirm the Commissioner's assessment.

¹⁸¹ *Case A39*, 69 ATC 227, *Case A40*, 69 ATC 229.

¹⁸² ITAA ss23F(16)(c), (d). *Case A39* 69 ATC 227.

interpreted by the Commissioner to exclude dividends received from exemption.¹⁸³

Income that in the Commissioner's opinion was derived by a superannuation fund indirectly from a dividend paid by a private company was to be deemed a dividend paid to the fund by that private company.¹⁸⁴ This prevented the interposition of trusts or partnerships between a private company paying a dividend and a superannuation fund. This sub-section was also dependent upon the opinion of the Commissioner.

At the time that the legislation relating to the taxation of dividends received from private companies was introduced, legislation relating to income from non-arm's length transactions was introduced for the exclusion of this income from the exemption conferred by s 23F¹⁸⁵.

Income tax was imposed¹⁸⁶ on the taxable income of a superannuation fund that comprised:

- private company dividends derived directly or indirectly by a qualifying employees fund for which the Commissioner had not exercised his discretion to exempt the dividends from tax; and

¹⁸³ *Case A41* 69 ATC 233; *Case A57*, 69 ATC 420; *Case B15*, 70 ATC 61; *Case E56*, 73 ATC 442.

¹⁸⁴ ITAA s 23F(9), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. ITAA s 23F(17) as part of the s 23F substituted by *Income Tax Assessment Act 1965*, No 103 of 1965.

¹⁸⁵ ITAA s 23F(10), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. ITAA s 23F(18) as part of the s 23F substituted by *Income Tax Assessment Act 1965*, No 103 1965.
Case A15 69 ATC 89, the Board found that amount of interest on a loan was not excessive, having regard to the company's financial position at the time and its history of subsequent borrowings.

¹⁸⁶ ITAA ss 23F(15)-(18); 121BA(2), (3), (4); 121 CB; from 1 July 1984, ITAA ss 23FB(13)-(15); from introduction of *OSSA*, ITAA ss 23FC(2)-(3). 23FD(2)-(4); from the introduction of ITAA pt IX, ss 273.
Rates in *Income Tax Act 1961 to 1975*; *Income Tax (Companies and Superannuation Funds) Act 1976 to 1985*; *Income Tax Rates Act 1986*.

- income derived from a transaction where the parties to the transaction were not dealing at arm's length with each other in relation to the transaction and where the income was greater than might have been expected had the parties been so dealing at arm's length.

The provisions in the *ITAA* pre-OSSA¹⁸⁷ that related to the factors that the Commissioner took into consideration to allow an exemption in the case of employer-sponsored fund and those for the initial period prior to the introduction of the taxing provisions were the same¹⁸⁸. For superannuation funds for self-employed persons, private company and non-arm's length income were assessable only where that income was derived after 29 October 1987.¹⁸⁹ For an approved deposit fund, private company and non-arm's length income were assessable only where that income was derived after 12 January 1987.¹⁹⁰

In assessing non-exempt private company dividends and non-arm's length income, as was the case with the provisions in the *ITAA* pre-OSSA, a deduction was allowable for expenditure to the extent that it was incurred in producing that income and was not of a private or capital nature.¹⁹¹ As was the case with the 30/20 rule, the trustee of a superannuation fund was not entitled to a rebate in respect of dividends from private companies and was not liable to pay provisional tax except on income assessed for non-compliance.

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¹⁸⁷ *ITAA* s 23F(16), (17).

¹⁸⁸ *ITAA* s 23FC(2)-(7).

¹⁸⁹ *ITAA* s 23FC(2)(a).

¹⁹⁰ *ITAA* s 23FD(2), (3), (4).

¹⁹¹ Deductions were allowed from the gross income for any 'losses and outgoings' incurred by the fund, to the extent to which they were incurred in gaining or producing the income concerned and were not of a private or capital nature.

¹⁹² *ITAA* s 121DD(c), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, amended by *Income Tax Assessment Act 1965*, No 103 1965. *Income Tax Assessment Act (No 2) 1977*, No 126 1977.

The introduction of *ITAA* Part IX¹⁹³ in 1988 included similar provisions for dividends paid by private companies and non-arm's length transactions, now known as 'special income'.¹⁹⁴ These provisions applied to complying superannuation funds, ADFs and PSTs.¹⁹⁵ Tax was applied to the 'special component'¹⁹⁶ of the taxable income at rates declared by Parliament.¹⁹⁷

ITAA Part IX was amended to clarify the application of the facts taken into consideration by the Commissioner when deciding if it would be reasonable not to treat a dividend as special income.¹⁹⁸ It was further amended to close a loophole in the law allowing certain distributions of trust income to superannuation entities made under non-arm's length arrangements to be taxed at the concessional rate. The amendments were strictly anti-avoidance in nature.¹⁹⁹ The amendments ensured that distributions of income from all trusts, other than where the superannuation entity had a fixed entitlement, were taxed at the non-concessional rate of tax.

ITAA s 121DD substituted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984, amended by *Taxation Laws Act (No 4) 1987*, No 138 1987.

193 Inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989 applicable to assessments for the year of income in which 1 July 1988 occurred and subsequent years.

194 *ITAA* s 273. It was in the same terms as former *ITAA* ss 23FC(2)-(5), ss 23FD(2)-(5) and the earlier provisions of former ss 23F(16)-(18).

TR 2006/7 Income Tax: Special Income derived by a complying superannuation fund, ... in relation to the year of income explains what amounts are considered to be 'special income' under *ITAA* s 273.

195 *ITAA* s 273(1).

196 Defined 'special component' in *ITAA* s 267(1) by referring to *ITAA* s 292 for a complying ADF, *ITAA* s 284 for a complying superannuation fund, *ITAA* s 298 for a PST. It was the amount remaining after deducting from the special income: (a) any allowable deductions that relate exclusively to the special income; and (b) so much of any other allowable deductions as, in the opinion of the Commissioner, may appropriately be related to the special income.

Included in 'special income' in *ITAA* s 273 were dividends from private companies, indirect dividends from private companies and income from non-arm's length transactions.

197 *Income Tax Rates Act 1986*.

198 'Paid-up value of shares' was amended to 'value of shares' by *Taxation Laws Amendment (Company Law Review) Act 1998*, No 63 1998. Lack of clarity had been noted in *Case A39*, 69 ATC 227, *Case A40*, 69 ATC 229.

199 Explanatory Memorandum to the *Superannuation Legislation Amendment Bill (No 2) 1999* [2.13] stated that the purpose of *ITAA* s 273 was to prevent income from being unduly diverted into superannuation entities as a means of sheltering that income from the normal rates of tax applying to other entities, particularly the marginal rates applying to individual taxpayers.

The amendments also ensured that income distributions, where the superannuation entity had a fixed entitlement to income from a trust, that the non-concessional rate of tax applied where the distribution was made in connection with a non-arm's length arrangement.²⁰⁰ The amendments extended the application of special income provisions to include non-share dividends, non-share equity interests and equity holders in the same way that it applied to dividends, shares and shareholders.²⁰¹

With the introduction of the *SISA* and *SISR* to replace the *OSSA* and *OSSR*, amendments to the *ITAA* reflected the change in the legislation.²⁰²

In 2007, *ITAA 97* division 295 rewrote and incorporated into *ITAA 97* the provisions of *ITAA* Part IX.²⁰³ The rewritten provisions were not intended to change the law as it previously operated under *ITAA* Part IX and continues to the current time in *ITAA 97*.²⁰⁴ 'Special Income' was renamed 'non-arm's length income' in the *ITAA 97*.²⁰⁵ In *ITAA* Part IX, the Commissioner had a discretion to decide that it was unreasonable that a dividend from a private company or non-arm's length income be treated as 'special income' where it was derived by a complying superannuation fund, complying approved deposit fund or a pooled superannuation trust. This was replaced with an objective test that the amount be

²⁰⁰ *ITAA* s 273(4) amended and *ITAA* s 273 (6), (7), (8), as inserted by *Superannuation Legislation Amendment Act (No 2) 1999*, No 96 1999.

²⁰¹ *ITAA* s 273(9), as inserted by *Superannuation Legislation Amendment Act (No 2) 1999*, No 96 1999.

²⁰² Amended by *Superannuation Industry (Supervision) Consequential Amendments Act 1993*, No 82 1993 applicable in relation to a fund for the 1994/1995 year of income of the fund and for all later years of income.

²⁰³ *ITAA 97* pt 3-30 Superannuation, as inserted by *Tax Laws Amendment (Simplified Superannuation) Act 2007*, No 9 2007 applicable to the 2007-2008 income year and later years.

²⁰⁴ *ITAA 97* pt 3-30 div 295 sub-div 295-H ss 295-545-555.

²⁰⁵ *ITAA 97* pt 3-30 s 295-550.

consistent with an ‘arm’s length dealing’.²⁰⁶ A taxpayer must self-assess as to whether a private company dividend is non-arm’s length income by reference to the specified factors.²⁰⁷

Non-arm’s length income²⁰⁸ is made up of the following amounts²⁰⁹:

- private company dividends, including ordinary or statutory income reasonably attributable to dividends (eg franking credits);²¹⁰
- ordinary or statutory income received from a non-arm’s length dealing;²¹¹
- income received from a trust in the capacity of a beneficiary, other than from a fixed entitlement (eg income from a discretionary trust);²¹²
- non-arm’s length income received in the capacity of a beneficiary from a fixed trust.²¹³

Non-arm’s length income also applies to non-share equity interests, equity holders and non-share dividends in the same way as it applies to shares, shareholders and dividends.²¹⁴

Ordinary or statutory income is ‘non-arm’s length income’ if it is derived by a superannuation entity from a scheme²¹⁵, the parties to

²⁰⁶ Explanatory Memorandum of the *Tax Laws Amendment (Simplification Superannuation) Act 2007*, No 9 2007 [3.78].

²⁰⁷ *ITAA 97* pt 3-30 s 295-550(3).

²⁰⁸ The ATO’s view is that an amount must be wholly non-arm’s length income or not be arm’s length income at all - *Taxation Ruling* TR 2006/7 [12].
Non-arm’s length component of the taxable income is taxed at the highest marginal rate set out in the *Income Tax Rates Act 1986*. *ITAA 97* s 295-545(2) defines the ‘non-arm’s length component’ for an income year as ‘the entity’s non-arm’s length income for that year less any deductions to the extent that they are attributable to that income’.

²⁰⁹ *ITAA 97* s 295-550.

²¹⁰ *ITAA 97* s 295-550(2)(a).

²¹¹ *ITAA 97* s 295-550(2)(b).

²¹² *ITAA 97* s 295-550(4).

²¹³ *ITAA 97* s 295-550(5).

²¹⁴ *ITAA 97* s 295-550(6).

which were not dealing with each other at arm's length in relation to the scheme.²¹⁶ The amount of income received must also be more than the amount that could have been expected if the parties had been dealing at arm's length.²¹⁷ Parties do not need to be at arm's length, provided that they are dealing at arm's length.

The consequence of non-compliance with the in-house asset rules is that the investment income of the fund is taxed at the rate of the imposition of tax declared by the Parliament.²¹⁸

The amendments indirectly protected the members' entitlements by ensuring that the trustees made appropriate investments to avoid unnecessary taxation of income of a superannuation fund.

3.4 Conclusion

The Federal Government's retirement income policy developed to address the emerging problem of an ageing population. The main objective was to ensure that all members of the population had an adequate and secure level of income in retirement. A secondary objective was to encourage people to save for their own retirement. The use of the tax legislation as a tool to assist the Federal

²¹⁵ ITAA 97 s 995-1 defines a scheme as '(a) any arrangement; or (b) any scheme, plan, proposal, action course of action or course of conduct, whether unilateral or otherwise.'

²¹⁶ *Taxation Ruling* TR 2006/7 [76]-[79], the ATO outlines that parties will be dealing with each other at arm's length if the independent minds and wills of the parties are applied and their dealing is a matter of real bargaining. The ability of one party to influence or control the other is suggestive that there may not be an arm's length dealing, although this is not determinative. The ATO relied on statements in the following cases to support these arm's length principles: *Re Hains (deceased)*; *Barnsdall v Federal Commissioner of Taxation* (1988) 81 ALR 173; *Australian Trade Commission v WA Meat Exports Pty Ltd* (1987) 75 ALR 287; *The Trustee for the Estate of the late AW Furse No 5 Will Trust v FC of T* (1990) 21 ATR 1123; *Granby Pty Ltd v Federal Commissioner of Taxation* (1995) 129 ALR 503.

²¹⁷ ITA 97 s 295-550(1).
Taxation Ruling TR 2006/7 [79]. [80], the ATO considers it is a question of fact as to whether an income amount is greater than if the parties had been dealing at arm's length. The level of investment risk the superannuation entity is exposed to is a relevant matter in determining this question.

²¹⁸ Rates applied: *Income Tax Act 1936 to 1975*; *Income Tax (Companies and Superannuation Funds) Act 1976 to 1985*; *Income Tax Rates Act 1986*.

Government to implement policy was successful in encouraging people to save for their retirements.

Initially, incentives were in the form of tax incentives. The increase in those in the workforce that had superannuation (32% in 1974 to 55% in 1988 of employees aged 15 to 64)²¹⁹ prior to the introduction of compulsory contributions is an indication that the tax incentives were working. The question of whether the members' benefits were in fact secure and available for them is addressed in Chapters 4 and 5 and forms the basis for the evolution of the regulation of superannuation funds. With the introduction of compulsory contributions, the number of superannuation coverage increased to 91% of the workforce in 2000.²²⁰

The assets in superannuation funds increased from \$50 billion in 1983 to \$484 billion in 2000.²²¹

The development of the in-house asset rules with the legislation for special income combined to provide protection not only for the Revenue but also members' benefits. By reducing the opportunity for the trustees to invest in assets that were not at arm's length and that may have had conflicts of interest, the risk that superannuation fund assets may have been lost was minimized.

The introduction of taxes on superannuation funds, albeit at concessional rates, allowed the Federal Government to continue to provide the tax incentives which had been successful in encouraging people to save for their retirement.

The Federal Government's use of the superannuation funds for general Revenue purposes has been highlighted. It also

²¹⁹ See Chapter 1 n 69.

²²⁰ ABS '2000 Survey of Employment Arrangements and Superannuation, Superannuation, Australia.

²²¹ See above n 109.

demonstrates the conflict that the Federal Government may have in determining the implementation of its policies. It used a percentage of superannuation funds' investments to finance its public works program²²² and imposed an additional charge on high income earners,²²³ ie reduced tax incentives, in order to reduce the budget deficit.

Non-compliance of superannuation funds with the requirements for the concessional treatment resulted in the application of non-concessional rates of tax. Whilst this imposition of non-concessional rates of tax acted as an incentive for superannuation fund trustees to comply with the provisions relating to members' benefits, it was members who were ultimately penalised by a reduction in their savings.

The Federal Government's concern for the security of members' benefits resulted in enquiry into improved regulation. This led to the evolution of the regulation of superannuation funds. It had been proven that the tax incentives were successful. The protection of members' benefits for their retirement and making trustees accountable for their responsibilities were the next steps to be taken in implementing the Federal Government's retirement income policy.

²²² The 30/20 rule. See [3.3.1].

²²³ Contribution surcharge. See [3.2.2.1].

CHAPTER 4

REGULATION

SUPERANNUATION FUNDS FOR EMPLOYEES

Chapter 2 analysed the evolution of the original basic trust structure of a superannuation fund to a 'statutory trust'. This was achieved by the development of the definition of 'superannuation fund'.

Chapter 3 detailed the exempt and concessional tax treatment of superannuation funds, which was the incentive provided by the Federal Government to encourage people to save for their retirement. It showed that this strategy was successful.

This Chapter focuses on regulation governing superannuation funds for employees during the period 1936 to 1986. It analyses the provisions of the *Income Tax Assessment Act*¹ ('ITAA') as they related to superannuation funds established for the benefit of employees of both the private and public sectors, from the introduction of the *ITAA* to the introduction of the *Occupational Superannuation Standards Act* ('OSSA')² in 1987. The analysis identifies issues arising from the interpretation of the requirements that were essential for exemption from income tax of the income of these funds. Taxpayers and their advisers interpreted the provisions to access the benefits of the exemption for superannuation funds in ways unintended by the Federal Government. This resulted in abuse of the provisions underlying Government policy to encourage saving for retirement. When the Commissioner challenged the

¹ The title of the income tax legislation from 2 June 1936 to 13 December 1950 was *Income Tax Assessment Act 1936*. From 14 December 1950 to 13 December 1965, the title was *Income Tax and Social Services Contribution Assessment Act 1936*. From 14 December 1965, the title reverted back to *Income Tax Assessment Act 1936*. 'ITAA' refers to both titles used at the different times.

² *Occupational Superannuation Standards Act 1987*, No 97 1987.

implementation of the provisions by taxpayers, the taxpayers had relied on unintended interpretations of the legislation. This accentuated the inadequacies of the provisions.

This Chapter contributes substantially to proving that the evolution of the regulation has been consistent with the Federal Government's policy intent to encourage people to save for their own retirement by protecting members' benefits and by making trustees accountable.

4.1 Background

This section sets out the detail of the regulation, issues and interpretation required for subsequent analysis. During the period 1936 to 1986, the Commissioner of Taxation had the general administration under the *ITAA*. This administration included the authority to exempt superannuation funds from taxation.³ Various Trustee Acts enacted by the various States of Australia regulated the establishment and maintenance of trusts.⁴

During the years 1936 to 1964, a general provision in the *ITAA*, s 23(j)(i), provided exemption from income tax for superannuation funds providing benefits for employees. This included employees of both the private and public sectors.

In 1961, a qualification to the exemption was introduced. For a superannuation fund's income to be exempted from income tax, the trustee of the fund must have invested a specified proportion of its assets in public securities. The relevant provisions were widely known as 'the 30/20 rule'⁵. They applied to both s 23(j)(i) and

³ *ITAA* s 8.

⁴ See Chapter 2 n 4.

⁵ *ITAA* div 9B - Superannuation Funds, ss 121B-121E, as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961. The 30/20 rule was included in this Division in ss 121C(1)-(12), effective from 1 March 1961.

23(ja) ⁶. The definition of ‘superannuation fund’ to which the 30/20 rule applied excluded superannuation funds established for the public sector.⁷ This exclusion continued to the abolition of the rule on 30 June 1984.⁸

From 1964, there were a number of amendments to the requirements for compliance by superannuation funds to be eligible for exemption from income tax. *ITAA* ss 23F⁹ and 23(jaa)¹⁰ replaced s 23(j)(i)¹¹. Section 23F regulated superannuation funds established for the benefit of employees and their dependents. Section 23(jaa) regulated superannuation funds established for employees of the public sector.

Section 23F was repealed effective from the beginning of the 1965-66 income year. New provisions for s 23F were substituted in the *ITAA*.¹² Some paragraphs had the same numbers, while others were altered to allow for the insertion of additional paragraphs. There

The validity of the insertion of Division 9B was challenged in *Fairfax v FC of T* [1965] 14 ATD 135 as being a law not with respect to taxation but promoting investment in public securities. It was held that the enactment was valid.

⁶ Superannuation funds established for self-employed persons.

ITAA s 23(ja), as inserted by amendment *Income Tax and Social Services Contribution Assessment Act (No 3) 1952*, No 90 1952, Date of Assent, commencement 18 November 1952.

⁷ *ITAA* s 121B (definition of ‘superannuation fund’, as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961).

⁸ Repealed by *Taxation Laws Amendment Act 1985*, No 49 1985.

⁹ Exemption of income of superannuation funds established for the benefit of employees. *ITAA* s 23F, as inserted by amendment *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, Date of Assent, commencement 23 November 1964.

¹⁰ Statutory, government and semi-government superannuation, etc funds. *ITAA* s 23(jaa), as inserted by amendment *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, Date of Assent, commencement 23 November 1964.

¹¹ *ITAA* s 23(j)(i) as repealed by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, Date of Assent, commencement 23 November 1964.

¹² *ITAA* s 23F, as repealed by and *ITAA* s 23F, as inserted *Income Tax Assessment Act 1965*, No 103 1965.

were further amendments to section 23F.¹³

The in-house asset rules replaced the 30/20 rules on their abolition in 1984. The in-house asset rules limited the proportion of the fund's assets that could be lent to or invested in the sponsoring employer or an associate of such an employer.¹⁴ In-house assets of a fund were those assets that consisted of loans to or investments¹⁵ in an employer-sponsor¹⁶ or an associate¹⁷ of an employer-sponsor.

In 1964, in response to the recommendations of Report of the Commonwealth Committee of Taxation,¹⁸ further limitations excluded some income of superannuation funds under specific circumstances from the exemption from income tax. These sources of income were dividends received from private companies and income was excluded from the exemption if the parties to the transaction giving rise to the income were not dealing with each other at arm's length and the income was greater than that which

¹³ ITAA s 23F, as amended by *Income Tax Assessment Act 1973*, No 51 1973, *Income Tax Laws Amendment Act 1981*, No 108 1981, *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

¹⁴ ITAA ss 121C(4), (5), as inserted by *Taxation Laws Amendment Act (No 2) 1985* No 123 1985.

¹⁵ ITAA s 121C(1) (definition of 'investment' as any mode of application of money for the purpose of gaining interest, income or profit).

¹⁶ ITAA s 121C(2)(a). An employer who contributed to a superannuation fund for the benefit of an employee (including a director) or dependants of an employee was treated as an employer-sponsor of the fund.

ITAA s 121C(2)(b). A company controlled by the employer and which contributed to the fund was also treated as an employer-sponsor.

ITAA s 121C(3). Where the employer was a company, any person connected with the employer company and who contributed was connected with a corporate employer where:

- the person has a controlling interest in the employer;
- the person was a company in which the controlling interest was held by a person who had a controlling interest in the employer; or
- the person was the beneficial owner of shares in the employer.

¹⁷ ITAA s 121C(1) referred to s 26AAB for the definition of 'associate'. In broad terms ITAA s 26AAB(14) defines any person who, by reason of business or family connections, as associated with a particular person.

¹⁸ Commonwealth Committee on Taxation, Commonwealth Government of Australia, *Report of the Commonwealth Committee on Taxation* (1961), 'Ligertwood Report' 156 [744].

might have been expected to have been derived from the transaction if those parties had been dealing at arm's length.¹⁹

Section 23FC was substituted for s 23F, first applicable to assessments for the year of income commencing 1 July 1986.²⁰ This exemption provision of *ITAA* was substituted to coincide with the introduction of *OSSA*²¹ and the *Occupational Superannuation Standards Regulations ('OSSR')*²². This is the subject of Chapter 6.

Section 23(jaa) allowed exemption from tax for the income of a provident, benefit, superannuation or retirement fund established by an Act, a State Act or an Ordinance of a Territory, or a local government body or by other public authorities established by similar means. These funds were referred to as public sector plans and related to employees of –

- the Australian government;
- the government of a State or Territory;
- a local government body;
- a public authority; or
- a university.

¹⁹ Inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. See Chapter 3 [3.3.3].

²⁰ *ITAA* s 23F, as repealed by and *ITAA* s 23FC, as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987, Date of Assent 18 December 1987.

²¹ *Occupational Superannuation Standards Act 1987*, No 97 1987, Date of Assent 5 November 1987, commencement 21 December 1987 but in most respects were deemed to apply from 1 July 1986.

OSSA s 3(1) (definition of 'year of income', in relation to a fund, means a period that is, for the purposes of the *ITAA*, the year of income of the fund that commenced on 1 July 1986 or a subsequent year of income).

OSSA s 4 sets out the application of *OSSA* in relation to periods before its commencement: *Taxation Laws Amendment Act (No 4) 1987*.

²² Commonwealth of Australia, *Occupational Superannuation Standards Regulations*, Statutory Rules 1987 No 322, 22 December 1987. Commencement of some regulations was 1 July 1986, some regulations applied from 1 July 1987, regulation 10 on 22 December 1986.

4.2 Section 23(j)(i) Superannuation Funds

The first provision of the *ITAA* to allow exemption of income from income tax by a superannuation fund was s 23(j)(i). *ITAA* s 23(j)(i) provided exemption from income tax:

the income of the following funds, provided that the particular fund is being applied for the purpose for which it was established -

- (i) a provident, benefit or superannuation fund established for the benefit of employees;

....

As the provision applied to all funds established for the benefit of employees, it included exemption of income from income tax of public sector plans established to provide superannuation for employees.

No reference is made in s 23 requiring a fund to be established in Australia. It would appear that there would have been no objection to exemption under section 23(j) being applied to a fund established outside Australia.²³

4.2.1 *Challenges of application of section 23(j)(i) by the Commissioner*

When the Commissioner and a taxpayer failed to agree on the interpretation or application of the requirements of the provisions of the income tax legislation, the taxpayer had the right to lodge an objection with the Commissioner against an assessment.²⁴ The taxpayer had a further right of review or appeal if it was dissatisfied with the decision made by the Commissioner. The review could be

²³ *University of Birmingham v FC of T, Epson College v FC of T* (1938) 5 ATD 63.

²⁴ *ITAA* ss 185, 187.

before a Board of Review.²⁵ The appeal could be referred to a court.²⁶

In a number of decisions, the High Court established the principles for determining whether a fund is established, the purpose for which a fund is established and whether it is being applied for that purpose.²⁷ In some instances, different interpretations by the Judges of what were the relevant issues of circumstances of the case under appeal revealed different inadequacies in the legislation. These different interpretations are discussed in the following analysis.

For the application of the exemption from income tax by a superannuation fund under s 23(j)(i), each component of the section must be complied with cumulatively in the following order.²⁸

1. Has a superannuation fund been established?
2. Is the superannuation fund for the benefit of employees?
3. Is the superannuation fund being applied for the benefit of employees?

Judges identified factors relevant to determining these issues during the course of cases before the court. These factors were:

²⁵ ITAA ss 192–195.

²⁶ ITAA ss 196–202.

²⁷ *Mahoney v Commissioner of Taxation* (1965) 39 ALJR 62; *Mahoney v Federal Commissioner of Taxation* (1967) 14 ATD 519; *Compton v Federal Commissioner of Taxation* (1965) 39 ALJR 400; *Compton v Federal Commissioner of Taxation (No 2)* (1966) 14 ATD 295; *Associated Provident Funds Pty Ltd v Federal Commissioner of Taxation* (1966) 14 ATD 333; *Rollason v Commissioner of Taxation* (1966) 121 CLR 45; *Dricald Pty Ltd v Commissioner of Taxation of the Commonwealth of Australia* (1968) 121 CLR 45.

The principles established in these cases were cited and relied on in the following cases: *Raymor Contractors Pty Ltd v FC of T* (1991) 21 ATR 1410; *FC of T v Roche & Ors* (1991) ATC 024; *Walstern Pty Ltd v FC of T* (2003) 54 ATR 423; *Cameron Brae Pty Ltd v FC of T* (2007) ATC 4936.

²⁸ *Mahoney v Commissioner of Taxation* (1965) 39 ALJR 62.

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- the language and terms of the trust deed;²⁹
 - any underlying or alternate motivation for establishing the superannuation fund established for the benefit of employees;³⁰
 - the payment and security of members' benefits;³¹
 - identifying income of a superannuation fund not eligible for exemption from income tax³².

Each question will be considered and deliberations by the Judges in cases relevant to the question will be discussed.

The analysis of each question will demonstrate the inadequacies of the provisions and identify factors relevant to determining whether the requirements of the legislation have been complied with for exemption from income tax. It will identify the inadequacies in the legislation that put the members' entitlements at risk and demonstrate what amendments to the legislation were necessary to protect the members' entitlements for their retirement.

4.2.1.1 *What determined whether a fund was established?*

In deciding if a provident, benefit or superannuation fund was eligible for the application of the exemption under s 23(j)(i), the first issue to be determined was whether a fund was established. The establishment of a fund as a trust is the first step of providing the protection of the members' entitlements.

²⁹ *Mahoney v Commissioner of Taxation* (1965) 39 ALJR 62; *Compton v Federal Commissioner of Taxation* (1966) 14 ATD 295.

³⁰ *Associated Provident Funds Pty Ltd v Federal Commissioner of Taxation* (1966) 14 ATD 333.

³¹ *Ibid.*

³² *Rollason v Commissioner of Taxation* (1966) 121 CLR 45.

A superannuation fund is a trust.³³ For the establishment of a trust, in addition to the appropriate parties being involved in the creation of a trust³⁴, there must be certainty in three matters:

1. intention to create a trust and to impose an equitable obligation on terms that are certain;
2. the property to be the subject of the trust; and
3. the objectives of the trust.³⁵

In summary, actions without the underlying intention to create a trust with terms for a trustee to comply will not be effective. Isaac J in *Commissioner of Stamps Duties (Qld) v Jolliffe* said that ‘intention alone will not constitute a trust obligation, so mere conduct without such intention is ineffectual to impose it’.³⁶

For a superannuation fund to be a trust, it had to comply with these requirements to establish a trust. The trust deed evidenced the intention to establish a superannuation fund. The trustee must be obliged in the trust deed to give effect to the intention. Property to establish the trust must be identified. The ATO required the terms and the objectives of the trust to be defined in the trust deed. It was the practice of the ATO to undertake a detailed examination of the trust deed. The subsequent approval by the ATO referred only to confirming the satisfaction of the formal requirements of the *ITAA*.³⁷

³³ See Chapter 2 for the discussion about superannuation funds as trusts.

³⁴ The trustee and the beneficiary together with trust property. H A J Ford & W A Lee, *Principles of the Law of Trust* (The Law Book Company Limited, 1983) 3.

³⁵ Ibid 63.

³⁶ (1920) 28 CLR 178, 189.

³⁷ In 1985, the ATO abandoned this procedure. The Commissioner introduced procedures for:

- (i) the amendments to trust deeds (Taxation Ruling IT 2067 paragraphs 48-49, effective date 1/7/82); and
- (ii) establishment of trust deeds (Taxation Ruling IT 2188, dated 30/8/85. Taxation Ruling IT 2351 addressed questions resulting from problems arising from the implementation of Taxation Ruling IT 2188).

In some cases, when considering the establishment of a superannuation fund, the Judges held that it was sufficient for there to be an intention to create a superannuation fund, to create rights and have property contributed for the establishment of a superannuation fund for the purposes of exemption from income tax under s 23(j)(i).

In *Mahoney v Federal Commissioner of Taxation*³⁸, Owen J held that if a deed of trust, executed by an employer, was a document intended to create and did create rights and obligations and that an amount of money was paid to the fund, the onus of showing that a fund was established was discharged and it was not open to the court to go behind it and investigate the motives of the employer.³⁹

Taylor J in *Compton v Commissioner of Taxation of the Commonwealth*⁴⁰ approved of the view of Owen J expressed above in *Mahoney v FC of T* on the matter of the language of the deed and the establishment of a fund.⁴¹

In other cases, the Judges thought that other factors needed to be considered in determining if a superannuation fund had been established. Judges determined that the presence of an underlying or alternative motivation for establishing the superannuation fund must be considered.

In the appeal against the judgment of Owen J in *Mahoney v FC of T*, Kitto J concluded that, even though he was prepared to assume that under the provisions of the deed the fund may be properly

³⁸ (1965) 13 ATD 519.

³⁹ Ibid 525.

⁴⁰ (1966) 39 ALJR 400.

⁴¹ Ibid 402. Also confirmed: *Rollason v FC of T* (1966) 14 ATD 324; *Driclad Pty Ltd v FC of T* (1966) 121 CLR 45.

described as established for the benefit of employees, a pertinent fact in his deliberation was that 'no allocation of funds was ever made to an employee, no employee became a member, and the result was that no trust of a 'provident, benefit or superannuation' character ever took effect with respect to any part of the trust fund.'⁴²

In *Compton v Federal Commissioner of Taxation*⁴³, although Taylor J approved the view taken by Owen J expressed above in *Mahoney v FC of T*⁴⁴, his Honour said that, although the deed did not contemplate the establishment of a fund for the benefit of all of the employees of the company, its fundamental purpose was the establishment of a fund for the benefit of employees nominated as members of the fund. No attempt was made to nominate any employee as a member of the fund. This resulted in no fund being established.⁴⁵

In contrast, in *Associated Provident Funds Pty Ltd v FC of T*⁴⁶, on whether a fund was established, Windeyer J said that the contention that reading the trust deed alone to determine if a superannuation fund was established was a mistake because the deed must be read with a preconception of what such a fund was.⁴⁷ In this case, the powers of investment by the trustee in the trust deed included powers of investment that were like the objects of a trading company. They included extensive powers to deal in land that was subsequently the main activity of the trustee. Because of the activities of the trustee in other entities, it was inferred that land trading was always the intention for the

⁴² *Mahoney v Federal Commissioner of Taxation* (1967) 14 ATD 519, 522.

⁴³ (1965) 39 ALJR 400.

⁴⁴ (1965) 39 ALJR 62, 63.

⁴⁵ *Compton v Federal Commissioner of Taxation* (1965) 39 ALJR 400, 402.

⁴⁶ *Associated Provident Funds Pty Ltd v FC of T* (1966) 14 ATD 333, 340.

⁴⁷ *Ibid* 351.

establishment of the fund to take advantage of the tax concessions of the *ITAA*.⁴⁸

Windeyer J said:

... it is not enough to say that a fund governed by the provisions of a deed ... could be a superannuation fund within the meaning of the Act. For it to be so in fact the parties concerned must have intended that the deed should take effect and operate according to its tenor; that a fund should be set up subjected to the trusts of the deed; and that ... (the) trustee be bound to carry out those trusts. On the other hand, if the scheme, including the deed, was intended to be a mere facade behind which activities might be carried on which were not to be really directed to the stated purposes but to other ends, then the words of the deed should be disregarded.⁴⁹

In *Associated Provident Funds Pty Ltd v FC of T*⁵⁰, Counsel for the taxpayer argued that correspondence from the Deputy Commissioner amounted to recognition of the fund as a superannuation fund for the purposes of the *ITAA*. The correspondence advised the taxpayer that the trust deed submitted for approval by the Commissioner complied with requirements for contributions to the proposed fund to be allowed as deductions under *ITAA* s 66. Windeyer J said that whilst perhaps relevant to some incidental aspects of the matter, he did not regard the correspondence as binding on the Commissioner or as creating an estoppel against him. His Honour referred to a remark made by Kitto J in *Federal Commissioner of Taxation v Wade*⁵¹ that ‘no

⁴⁸ Ibid 352.

⁴⁹ Ibid 352.

⁵⁰ (1966) 14 ATD 333.

⁵¹ (1951) 9 ATD 337, 344.

conduct on the part of the Commissioner could operate as an estoppel against the operation of the Act'.⁵²

A summary of the findings of the courts in these cases indicate that for a trust to be established as a superannuation fund the following should be present:

1. an intention of the creator of the trust to create a superannuation fund;
2. documentation of the objectives and purpose of the superannuation fund;
3. language and definitions in the documentation supporting the objectives and purpose of the superannuation fund;
4. evidence of the initial property establishing the superannuation fund to be held on trust;
5. creation of membership of the superannuation fund by allocation of contributions to a member's benefit account.

The creation of a trust provided an environment in which the legislation regulating its maintenance could protect the members' entitlements.

4.2.1.2 What determined whether a fund was established for the benefit of employees?

Once it was concluded that a fund had been established, whether it was established for the benefit of employees must be determined. The intention of establishing a fund and identifying the entitlements for members was the second step of providing the protection for the entitlements.

Again, the language of the trust deed was relied upon. In some cases, the Judges accepted the general language and terms of the

⁵² *Associated Provident Funds Pty Ltd v FC of T* (1966) 14 ATD 333, 340.

trust deed. In other cases, they required the language to be more specific and restrictive than a general acknowledgement of the intention, the obligations of the trustee and the operations of the fund.

As set out below, whilst the trust deed may include the fundamental intention to create a superannuation fund for the benefit of employees, an underlying or alternative motivation identified in the trust deed may undermine the purported intention to create a superannuation fund. The actions of the trustee and the operations of the fund must support the fundamental intention of establishing a superannuation fund for the benefit of employees.

What evolved from determining if a fund was established for the benefit of employees was what was later to be known as ‘the sole purpose test’. The security of the members' benefits was also raised as an issue for consideration.

As stated above in *Mahoney v FC of T*⁵³ in reference to determining the establishment of a superannuation fund, Owen J said that whether a fund was a provident, benefit or superannuation fund established for the benefit of employees was a matter to be ‘determined from the language of the deed and its meaning could not vary according to the motives of those who established it’⁵⁴. His Honour held that the fact that, under the terms of the Deed, the employer had a complete and unfettered discretion to direct the administration and investments of the fund, did not detract from the fund having complied with the description of a provident,

⁵³ (1965) 13 ATD 519, 525.

⁵⁴ Owen J referred to *Keren Kayemeth Le Jisroel Ltd v Inland Revenue Commissioners* [1932] All ER Rep 971: House of Lords: Lord Tomlin, Lord Warrington, Lord Thankerton, Lord Macmillan and Lord Wright. For comparison of view see: *A & S Ruffy Pty Ltd v FC of T* (1958) 11 ATD 452; *National Deposit Friendly Society Trustees v Skegness Urban District Council* (1959) AC 293, per Lord Denning 320.

benefit or superannuation fund established for the benefit of employees.⁵⁵ That is to say the Deed did not have to be specific in its language in restricting the actions of the trustee and the operations of the fund.

In *Compton v Federal Commissioner of Taxation*⁵⁶, the trustee of the superannuation fund invested in a company associated with the employer and trustee. Evidence showed that the fund was established to create a distribution of substantial profits of the company without attracting liability to tax. Taylor J said, that if, under the terms of the deed, income was credited to an accumulation account and not to individual members, and

if ... it was intended by the deed that the bulk of the income should be accumulated and distributed only on a winding-up of the fund, it could scarcely be said that the fund was one established for the benefit of employees.⁵⁷

The Full Court in *Compton v Federal Commissioner of Taxation (No 2)*⁵⁸ affirmed the decision of Taylor J but on different grounds. Their Honours provided different reasons for their interpretation of why a fund was not established for the benefit of employees. Other Justices in subsequent cases and Members of the Board of Review with different sets of circumstances adopted these reasons.⁵⁹

A reason considered fatal to the application of the exemption in s 23(j)(i) was that a fund did not meet the criteria of being established as a ‘provident, benefit, superannuation or retirement fund’ if the deed establishing a fund contained a clause providing

⁵⁵ *Mahoney v FC of T* (1965) 13 ATD 519, 525-526.

⁵⁶ *Compton v Federal Commissioner of Taxation* (1965) 39 ALJR 400.

⁵⁷ *Ibid* 402-403.

⁵⁸ (1966) 14 ATD 295.

⁵⁹ *Mahoney v Federal Commissioner of Taxation* (1967) 14 ATD 519; *Driclad Pty Ltd v Commissioner of Taxation* 116 (1966) C.L.R 233; *Case L13* 79 ATC 72; *Case X60* 90 ATC 438; *Raymor Contractors Pty Ltd v FC of T* 91 ATC 4259; *Case X16* 90 ATC 180.

for a purpose in addition to benefits for employees. In this case, the trust deed provided for the creation of a reserve fund to meet future contingent liabilities of employers.

Menzies J took the view, as did Owen J, that, for a fund to comply with the requirements of s 23(j)(i), it had to be established exclusively for the benefit of employees and for no other purpose. For his reasons, his Honour referred to the context of s 23(j). For funds to be exempt from income tax under ss 23(j)(ii)⁶⁰ and (iii)⁶¹, they had to be established for the purposes enumerated in the provision and no other purpose.

The exclusiveness which I find in s 23 (j)(ii) and (iii) without any express limiting provision suggests I think, that a like exclusiveness is to be found in s 23 (j)(i), in which a similar pattern of language is to be found. Another consideration pointing in the same direction is the impossibility of establishing any satisfactory criterion to determine the character to be attributed to a fund which is in part to be used for the benefit of employees and in part for other purposes.⁶²

His Honour expressed the view that this construction of s 23(j)(i) would not deny its applicability to a fund containing provisions for the benefit of dependents of employees.⁶³

Owen J using the principle in the judgment of Windeyer J in *Randwick Corporation v Rutledge*⁶⁴ with which Dixon CJ and Fullagar and Kitto JJ agreed, stated a fund cannot properly be described as having been established by an employer for the benefit of his employees if under its terms the trustees are required, in certain events, to apply the whole or some part of the

⁶⁰ ITAA s 23(j)(ii) – ‘a fund established by will or instrument of trust for public charitable purposes’.

⁶¹ ITAA s 23(j)(iii) – ‘a fund established for the purpose of enabling scientific research to be conducted by or in conjunction with a public university or public hospital’.

⁶² *Compton v Federal Commissioner of Taxation (No 2)* (1966) 14 ATD 295, 299.

⁶³ Ibid.

⁶⁴ (1959) 102 CLR 54.

trust property for the benefit of the employer, thereby reducing or extinguishing benefits which the trust instrument would otherwise have given to the employee.⁶⁵

In the Appeal⁶⁶ by the trustees against the decision of Owen J in *Mahoney v FC of T*⁶⁷, Kitto, Taylor and Windeyer JJ determined that it was not enough for a fund to comply with the statutory description of a superannuation fund to attract the exemption under s 23(j)(i) for income.

Windeyer J stated that it is also necessary to look:

critically at the terms of the trust deed at what it required and what it permitted - that is to say to see in what ways the trustees might, without any breach of the trusts it imposes, apply the trust property. Unless they were confined to applying the fund in ways consonant with it being a provident, benefit or superannuation fund for the benefit of employees, it cannot answer that description. In other words, if they could, keep within the terms of the trust, apply the fund or any portion thereof to purposes foreign to the true purpose of such a fund, then it would not be such a fund.⁶⁸

His Honour concluded that:

A fund held upon trusts which do not assure to any employee or employees some benefit more certain and secure than do the trusts of this deed, is I think, not a fund established for the benefit of employees.⁶⁹

Taylor J referred to the decision in *Compton v Commissioner of Taxation*⁷⁰ in which it was decided that:

⁶⁵ (1966) 14 ATD 295, 301.

⁶⁶ (1967) 14 ATD 519.

⁶⁷ (1965) 8 ATD 519.

⁶⁸ (1967) 14 ATD 519, 527.

⁶⁹ Ibid.

⁷⁰ (1966) 14 ATD 295.

a fund established partly for the purpose of giving superannuation benefits to employees and partly for the benefit of indemnifying their employer against future possible liabilities for long service leave is not answering the statutory description, it must, as I read the decision, be a fund established *exclusively* for the benefit of employees.⁷¹

His Honour held that on the facts of the case the fund was not a superannuation, provident or benefit fund for the benefit of employees.

Taylor and Windeyer JJ held that the fund was not at any relevant time being applied for the benefits of employees.⁷²

Another reason indentified as fatal to the application of the exemption of s 23(j)(i) was the use of the fund for earning operating income in a tax free environment.

In *Associated Provident Funds Pty Ltd v FC of T*⁷³, the trust deed allowed for money or investments to be furnished to the trustee 'by means of contribution or otherwise' to be held by it upon the trusts of the deed. Potential members of the superannuation fund transferred shares in the employer company, a company dealing and owning land, to the trustee.⁷⁴ The potential members and others made application to become members of the fund and were accepted. Contributions were made for them. All contributions received by the superannuation fund for the employees were subsequently lent to the employer at a specified rate of interest as they were received.

⁷¹ (1967) 14 ATD 519, 524.

⁷² Ibid 528.

⁷³ (1966) 14 ATD 333.

⁷⁴ Ibid 343.

After a period of five years, the assets of the fund did not represent the accumulated contributions made by employees and their employers. The accumulations in the fund represented profits made by dealing in land facilitated by money lent to the fund by the employer and associated companies, borrowed from the bank and from the initial investment of shares acquired from the then potential members.⁷⁵

The issue, in addition to whether the fund was ‘a superannuation fund established for the benefits of employees’ and was being applied for the purpose for which it was established within the meaning of s 23(j)(i), was whether the money said to be income of the fund was in fact income of such a fund.

Windeyer J said:

I have come to the conclusion that there is no essential single attribute of a superannuation fund established for the benefit of employees except that it must be a fund *bona fide* devoted as its sole purpose to providing for employees who are participating in money benefits (or benefits having a monetary value) upon their reaching a prescribed age. In this connexion ‘fund’, I take it, ordinarily means money (or investments) set aside and invested, the surplus income therefrom being capitalised.⁷⁶

In conclusion, His Honour said:

The inference I draw from the evidence as a whole is that there never was in truth a superannuation fund established for the benefit of employees. I should add that if there was such a fund established it was not in my view being applied at any time for the purposes for which it was established, that is to say for the benefit of employees according to its terms: *Mahoney v Federal*

⁷⁵ Ibid 344-345.

⁷⁶ (1966) 14 ATD 333, 351.

*Commissioner of Taxation, supra, Compton v Commissioner of Taxation.*⁷⁷

In *Rollason v Commissioner of Taxation of the Commonwealth of Australia*⁷⁸, the Commissioner took the view that the fund was established to enable contributing companies to avoid income tax upon a substantial part of their profits by making contributions to the fund. His Honour found that the investments made by the trustees were within their investment powers.

Taylor J concluded that the trust deed for the Marine Plastics Superannuation Fund set up two funds, held by the same trustees and administered together but subject to an obligation of appropriate accounting to keep separate the identity of the 'A' section fund and the 'B' section fund.

His Honour set aside the part of the assessment disallowed by the Commissioner on the basis that

s 23(j) is not concerned with the reasons which induce a company to constitute a superannuation fund; it is concerned with the purposes to which the fund is, or is to be, devoted and in the present case these are ascertainable from, and only from, the provisions of the trust deed.⁷⁹

His Honour found that 'A' section of the fund was established for the benefit of employees.⁸⁰

His Honour, relying on the reasons for his decision in *Driclad Pty Ltd v Federal Commissioner of Taxation*⁸¹, held that 'B' section of the fund was not established for the benefit of employees. Because

⁷⁷ Ibid 352.

⁷⁸ (1966) 14 ATD 324, 325.

⁷⁹ Ibid 325.

⁸⁰ Ibid.

⁸¹ (1966) 14 ATD 302, 309.

the trust deed provided for the investment of moneys standing to the credit of an individual member for his individual and sole benefit, not the fund, a fund exempt pursuant to *ITAA* s 23(j)(i) was not established.⁸²

Subsequently, in the appeal to the Full Court⁸³, Barwick CJ and Kitto J agreed with Taylor J that two funds had been set up and that 'A' section of the fund was exempt under s 23(j). With respect to 'B' section of the fund, their Honours concluded that if a fund was established for the benefit of employees only, there was no doubt that the income was being applied for these purposes, notwithstanding that the 'B' section employees were an exclusive class of employees.⁸⁴ They said they would consider the income of the fund would not be within s 23(j)(i) if the fund had been established not only to provide benefits for employees but also for another purpose - eg if the deed provided for contributions to the fund to be returned as loans to the contributors. Their Honours differentiated between the term 'authorised' (the term used in this case) and 'required'.⁸⁵

Menzies and McTiernan JJ agreed entirely with the reasons published by the Chief Justice and Kitto J upon the questions of substance.⁸⁶

In summary, the consensus of opinions of the Justices in these cases indicated that for a trust to be established as a superannuation fund for the benefit of employees, the trust deed must document this specific purpose and no other. Application of

⁸² (1966) 14 ATD 324, 324.

⁸³ (1968) ATD 15 179. Appellants: Driclad Pty Ltd, Marine Plastic Co. Pty. Limited and Rollason.

⁸⁴ Ibid 183.

⁸⁵ Ibid.

⁸⁶ Ibid 184.

the terms of the trust deed by the trustees was interpreted as evidence of intention. This restriction of specific purpose and its application prohibited the trustee from putting the members' benefits in a fund at risk.

4.2.1.3 *What determined whether a fund was 'being applied for' the benefit of employees?*

Isaacs J said in *Trustees, Executors and Agency Co. Ltd v Federal Commissioner of Taxation*⁸⁷ that the phrase 'being applied for' must be given 'some elasticity'. Accumulation of funds for a purpose that cannot be achieved in a particular income year can still satisfy the term 'being applied for'.

'Being applied' is as true of the first step in the process as of the last. The Commissioner, in examining the facts, can judge of the reality of the first step, and of its actual standing, as carrying out the provisions of the trust.⁸⁸

In determining whether a fund was, during the year of income, being applied for the purpose for which it was established, Owen J in *Mahoney v FC of T* said that:

it is permissible to look at the circumstances leading up to the establishment of the fund, the terms of the deed under which it was managed and controlled, the use made of the powers and discretions conferred by the deed, the extent to which benefits were received from the fund and the extent to which it was used to benefit persons who were not employees.⁸⁹

and not to limit the inquiry 'to the particular year of income' in which the fund claimed exemption from income tax.⁹⁰

His Honour referred to Isaac J's statement above, that 'being applied for' must be given some elasticity and confirmed that the

⁸⁷ (1917) 23 CLR 476, 587.

⁸⁸ Ibid.

⁸⁹ (1965) 13 ATD 519, 526.

⁹⁰ Ibid.

inquiry relating to the application of a fund for the benefit of employees need not be limited ‘to the particular year of income’ in respect of which exemption under s 23(j) was claimed.⁹¹

His Honour said that because the trustees of a fund invest its money in accordance with the trust deed does not mean that the fund is being applied for the benefit of employees. He referred to *Re Whiteley, Whiteley v Learoyd*⁹² in which Lindley LJ said that the trustees must conduct the business of the fund with the same care which a prudent, honest man would do for the benefit of those for whom they are responsible. This is a relevant circumstance in determining if the fund is being applied for the benefit of employees.⁹³

In this case, the trustee of the fund purchased shares in the employer company that subsequently paid a dividend on these shares to the employer. The trustee lent money to the employer to participate in a ‘highly speculative venture’, failed to register a debenture securing the repayment of the loan and did not take any steps to recover the money lent or the interest accrued. The employer made no allocation of the fund to any employee so that the fund remained without ‘members’. It was held that the fund was in fact being applied for the benefit of the employer company or others rather than for the benefit of employees.⁹⁴

The same finding was reached with the application of similar principles in *Compton’s case*⁹⁵ and *Associated Provident Fund’s case*⁹⁶.

⁹¹ Ibid.

⁹² (1886) 33 Ch. D. 347, 355.

⁹³ (1965) 13 ATD 519, 526.

⁹⁴ Ibid.

⁹⁵ (1966) 14 ATD 295.

A summary of the findings of the courts, from the cases above, indicated that in determining whether a superannuation fund is being applied for the benefit of employees the following should be considered:

1. are benefits being applied to others rather than employees;
2. are benefits available to a restricted a class of employees;
3. is the money earned the result of investing contributions for the benefit of employees;
4. is the motivation of the investment strategy to earn profits in a tax free environment?

The restricted application of the fund for the benefit of employees protected the integrity of the fund and was a method of protection for the members' entitlements.

4.2.2 *Inadequacies of s 23(j)(i) established by Court*

The inadequacies in s 23(j)(i) exposed by the Commissioner disallowing the exemption of income of a fund and the subsequent challenges in the courts, led to the Judges identifying principles to determine if a fund was for the benefit of employees. The following were identified in the cases above as pertinent factors to consider in determining the eligibility of the fund for exemption from income tax:

1. the circumstances leading up to and the motives for the establishment of the fund, including timing and tax consequences;
2. the terms of the trust deed establishing the fund and the application of the fund by the trustee for the benefit of members, including:
 - (i) whether the fund was exclusively for benefit of employees or partly for the benefit of the employer;

⁹⁶ (1966) 14 ATD 333.

- (ii) the powers and discretions of the employer contributing to the fund to:
 - (a) direct investment of funds;
 - (b) allocate sums of the funds to members;
 - (c) remove and replace the trustee; and
 - (d) wind up the fund;
 - (iii) the power of the trustee, at its discretion, to:
 - (a) accept or decline an application for membership;
 - (b) pay benefits;
 - (c) invest in the contributing employer; and
 - (d) lend money to the contributing employer and related parties with or without security and/or interest;
 - (e) borrow money for acquisition of assets; and
 - (f) wind up the fund;
 - (iv) the obligation of the trustee to:
 - (a) protect the assets of the fund;
 - (b) secure the interests of members; and
 - (c) advise members of the existence of the superannuation fund.
3. property to establish the trust was paid or transferred to the trustee;
 4. funds were allocated to member(s) to complete the establishment of the fund; and
 5. income was really for the benefit of members and not for tax effective purposes.

In addition to being pertinent factors in determining the eligibility of the fund for exemption from income tax, they were pertinent, either directly or indirectly, in providing and protecting benefits for employees for their retirement.

4.2.3 *Inadequacies of s 23(j)(i) identified by Government*

On 3 December 1959, the Federal Government appointed a committee to enquire into certain aspects of the taxation laws of the Commonwealth. This committee became known as the Ligertwood Committee ('Committee').⁹⁷ The main task of the Committee was to ascertain anomalies, inconsistencies and complexities in the law of income tax and to recommend remedies. Matters of Government policy arising from economic, social or overall revenue considerations were outside the sphere of the enquiry.

The Committee relied on data provided by the Commissioner of Taxation. It did not access any taxpayer's income tax return or assessment. The Commissioner provided technical and statistical information and comments on various proposals. Whilst the matters before the courts were heard after the Committee made public its report and recommendations, the Commissioner would have included the anomalies that formed the basis of the challenges between taxpayers and the Commissioner to the Committee. The Committee also had access to the cases on which the Judges relied in their deliberations for the unpublished cases. The recommendations made by the Committee reinforced the underlying principles developed in earlier cases. This can be seen in the following analysis in that courts retained the basic meanings giving effect to those purposes in their interpretation in the new legislation. Therefore in the analysis, reference to pre-Ligertwood cases is made as they have been supported subsequently and demonstrate that the purpose has always been to regulate funds for the benefit of members and to make the trustees accountable for their responsibilities.

⁹⁷ Commonwealth Committee on Taxation, Commonwealth Government of Australia, *Report of the Commonwealth Committee on Taxation* (1961).

Other material relied on by the Committee was in the Report of the Royal Commissioner on Taxation 1932-1934 ('Ferguson Commission') and the numerous Reports on individual aspects of income tax law by the Committee on Taxation 1950-1954 ('Spooner Committee').⁹⁸

The Committee recognised the problem generally arising from schemes of tax avoidance. In particular, schemes exploited the favourable treatment of superannuation funds. The Committee commented that there were numerous ways by which a taxpayer could constitute a superannuation fund in which the income would accrue to the taxpayer. In the ordinary course of events the taxpayer in virtually a tax free form could receive that income. This anomaly was considered to be more serious if the terms of the fund, or other circumstances, enabled the taxpayer to withdraw his benefits from the fund before reaching the normal retiring age. Some of the schemes identified by the Committee were:⁹⁹

- contributions to a superannuation fund made for persons not connected with the taxpayer;
- forfeited benefits distributed to remaining employees in an inequitable manner;
- multiple contributions made to a superannuation fund for one employee by associated companies;
- interposing companies to maximize deductions for an employee who was a shareholder;
- nominal duties of a director to maximize the annual amount set aside for his benefit in a superannuation fund with the company obtaining a tax deduction;
- purchase of shares with special rights by a superannuation fund in an employer. This resulted in the dividends paid to the superannuation fund being exempt from income tax, the

⁹⁸ Ibid xi and xii.

⁹⁹ Ibid 151-156.

company avoiding undistributed income tax¹⁰⁰ and the income in the superannuation fund accumulating for the benefit of directors on their retirement;

- interest free loans being made by a private company to a superannuation fund which invested the proceeds. Income from the investment was exempt from income tax and was accumulated for the directors of the private company.

Although these schemes were not illegal, it was recognised that they were inequitable.¹⁰¹ The Committee found that the diminution or avoidance of the tax liability by the ingenious use of the provisions of the *ITAA* and of the general law by taxpayers resulted in a loss of Federal Government's revenue which had to be made good by the remaining taxpayers who either did not have the same knowledge or opportunity of avoiding tax or were unwilling to engage in schemes to thwart the apparent intentions of the legislation.¹⁰²

To overcome the use of artificial devices for avoidance of tax by exploiting the provisions for the exemption or partial exemption of income of a superannuation fund from income tax, the Committee recommended specific conditions and limitations to the application of these provisions.¹⁰³ The recommendations provided for a series of tests to guide the Commissioner of Taxation as to which funds

¹⁰⁰ *ITAA* s 104 required additional tax to be paid if a company was deemed to have made insufficient distribution in relation to a year of income. *ITAA* s 104, later amended a number of times and repealed. *ITAA* s 104, as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1952*, No 90 1952. This requirement was phased out commencing 1 July 1986.

¹⁰¹ The Ligertwood Report, see above n 97, xii.

¹⁰² Ibid xiii.

¹⁰³ Ibid, 156-157.

should qualify for full exemption or which funds should be given a partial exemption.¹⁰⁴

In its report to the Federal Government, in relation to exemption from tax of income of superannuation funds, the Committee recommended:¹⁰⁵

that Section 23(j) should be amended to provide that
Subject to Division 9B the following income, except to the extent
that it represents:

- (i) dividends received from a private company within the meaning of Division 7 of Part III, of this Act; or
- (ii) other income received from a private company unless the Commissioner of Taxation is satisfied that the parties are at arm's length and that the income arises from a bona fide transaction made in the ordinary course of business,

shall be exempt from tax:

- (a) the income of a provident, benefit or superannuation fund in relation to which the Commissioner of Taxation is satisfied that
 - (i) it is a permanent fund established solely for the benefit of the employees of a business or group of business to the dependants of those employees, and primarily for the purpose of providing pensions or allowances on retirement or death of employees;
 - (ii) the rights of those employees or of their dependants to the whole of the capital and income of the fund are fully secured;
 - (iii) the entitlement of each individual beneficiary is defined, and has been communicated to the individual;
 - (iv) amounts remaining in the fund when a member forfeits rights, as a result of resignation or voluntary withdrawal from the fund, can only be used in reduction of employers' contributions or the provision of additional benefits for the remaining members of the fund on a basis which does not discriminate;

¹⁰⁴ Ibid.

¹⁰⁵ Ibid.

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- (v) the benefits to be provided under the fund are not excessive in amount, having regard to remuneration and length of service, or other special circumstances which, in the opinion of the Commissioner of Taxation, ought to be taken into account;
 - (vi) the capital of the fund from time to time is not substantially in excess of the amount needed to provide these or additional benefits reasonably required.
- (b) so much of the income of any other provident, benefit or superannuation fund established for the benefit of employees, being a fund that is being applied for the purposes for which it was established, as does not exceed the amount of income received by that fund during the year ended 30 June 1961, provided that where the income of the fund includes income derived by the trustees of the fund from carrying on a trade or business, the amount of income exempted from tax shall not exceed 10 per cent of the accumulated funds of the fund as at 30 June 1961.

Some of the recommendations made by the Committee in relation to superannuation were accepted and introduced commencing on 23 November 1964. The recommendations adopted were incorporated into a new section, *ITAA s 23F*, in an attempt to avoid any doubt in the interpretation of the application of the exemption provisions.

4.3 Section 23F Superannuation Funds

The Federal Government accepted some of the Committee's recommendations and others with variations¹⁰⁶. It did not accept

¹⁰⁶ Where the Federal Government considered a proposal overly severe, the recommendation was amended. For example, instead of dividends from private companies being excluded from exemption from income tax as recommended by the Committee, the inserted s 23F provided that Commissioner examine each individual case to determine whether that income should be taxed. Similarly, the Commissioner was to decide if parties to a transaction were not dealing at arm's length and tax the income accordingly. The Treasurer, 'Income Tax and Social Services Contribution Assessment Bill (No 3) 1964' (Second Reading Speech at the House of Representatives, Canberra). The Minister,

others for various reasons.¹⁰⁷ The recommendations for amendments to superannuation funds by the Committee fell into two categories. The first were designed to protect the Federal Government's revenue from the abuse by taxpayers. Unintended interpretations of the provisions in *ITAA s 23(j)(i)* allowed deductions for contributions to and exempting the income of superannuation funds from income tax. This resulted in leakage of revenue. The second category protected the entitlements of members.

The analysis that follows is limited to those recommendations adopted to protect the entitlements of members. It considers whether the amendments addressed the inadequacies of the former section providing the exemption, *s 23(j)(i)*, as highlighted by the courts and the Committee. It identifies which inadequacies have not been addressed and whether there were further inadequacies after the adoption of the recommendations.

4.3.1 Background

The recommendations of the Committee adopted were inserted as *s 23F* into the *ITAA* in 1964.¹⁰⁸ Section *23(j)(i)* was omitted from *ITAA*.¹⁰⁹ The exemption under *s 23F* was effectively a continuation of the exemption previously conferred under the more general provisions of *s 23(j)(i)* with additional specific compliance requirements as recommended by the Committee.

'Income Tax and Social Services Contribution Assessment Bill (No 3) 1964' (Second Reading Speech at the Senate, Canberra).

¹⁰⁷ The proposed method of taxing superannuation funds that did not satisfy the proposed test was rejected. An alternate method was adopted. The Treasurer, *Income Tax and Social Services Contribution Assessment Bill (No 3) 1964* (Second Reading Speech at the House of Representatives, Canberra). The Minister's *Income Tax and Social Services Contribution Assessment Bill (No 3) 1964* (Second Reading Speech at the Senate, Canberra).

¹⁰⁸ Exemption of income of superannuation funds established for the benefit of employees, as inserted by amendment *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, Date of Assent, commencement 23 November 1964.

¹⁰⁹ *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964.

The Federal Government adopted a recommendation of the Committee that the provisions authorise exemption of the income of a superannuation fund if the Commissioner was satisfied that certain tests were met. These tests prescribed by the Committee were generally followed in exemption provisions of the *ITAA*.

Section 23F was subsequently repealed in 1965 and a new s 23F inserted.¹¹⁰ In the original provisions in s 23F, the Commissioner had a discretionary power to allow the exemption section to apply even though all the tests had not been met. This appeared to make the provisions less rigid than the Committee recommended. However, this discretionary power of the Commissioner prohibited a trustee of a superannuation fund the right to appeal to a court against a decision of the Commissioner.¹¹¹ The new provisions withdrew the discretionary power in some instances. Other provisions in the substituted s 23F were of a technical nature and had the purpose of eliminating possible ambiguities.

The substituted s 23F is the basis of this analysis. Any reference to differences in the original s 23F is commented on in the footnotes if significant.

¹¹⁰ *ITAA* s 23F, as repealed by, new provisions for s 23F as inserted by *Income Tax Assessment Bill 1965*, No 103 1965. Date of Assent, commencement 14 December 1965. Later amended by *Income Tax Assessment Act 1973*, No 51 of 1973, *Income Tax Amendment Act 1981*, No 108 1981 and *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

¹¹¹ *ITAA* ss 23F(11), (18).
A person who was dissatisfied with a decision of the Commissioner might have it reviewed by a Board of Review. A Board's decision on the exercise of a discretionary power displaced that of the Commissioner. A taxpayer did not have the right to challenge this decision.
Where the exercise of a discretionary power was involved, a question in dispute would generally be referred to a Board of Review because the law entitles a Board of Review (but not a court) to substitute its opinion on the use of a discretionary power for the decision of the Commissioner. The courts do not exercise such a wide power in relation to the use of the discretionary powers of the Commissioner. A decision given by a Board of Review on any question of fact is final but there is a right of appeal to the High Court from a Board's decision on a question of law. Refer Public Information Bulletin ('PIB') No 1 published by the Office of the Commissioner of Taxation, Canberra in March 1965.

The requirements for eligibility for exemption from income tax were set out in *ITAA* ss 23F and 121C.¹¹² *ITAA* s 23F granted an exemption from tax¹¹³ for the income¹¹⁴ of a superannuation fund established by their employer¹¹⁵ for the benefit of employees¹¹⁶ or their dependants¹¹⁷ on their retirement where the fund satisfied all, ie cumulatively, the section's specified requirements¹¹⁸. There were additional requirements to be satisfied for exemption under *ITAA* s 23F. The exemption applied to all income of the fund, other than private company dividends¹¹⁹ and other non-arm's length income¹²⁰. *ITAA* s 121C provided another requirement to be complied with for exemption under s 23F.¹²¹ It involved the

¹¹² *ITAA* ss 23F(15), 121C(1)-(3).

¹¹³ *ITAA* s 23F(15). This exemption was initially granted by *ITAA* s 23F(7), renumbered to sub-section (13) by *Income Tax Assessment Act 1965*, No 103 1965 with the final exemption provision being *ITAA* s 23F(15), formal amendment by *Income Tax Laws Amendment Act 1981*, No 108 1981.

¹¹⁴ It was the income, not the entity, that received the exemption. The income, but for the exemption, would have been liable to tax. *Reid v FC of T* (1947) 3 ATD 255.

¹¹⁵ *ITAA* s 221A(1) (definition of an employer was defined:
a person who pays or is liable to pay any salary or wages and includes –
(a) in the case of an unincorporated body of persons other than a partnership - the manager or other principal officer of that body, and
(b) in the case of a partnership - each partner,
and, except in relation to the imposition of a penalty –
(c) also includes the Commonwealth and an authority of the Commonwealth; and
(d) where the Governor-General has entered into an arrangement with the Governor in Council of a State in accordance with section 221B subject to the terms of the arrangement, also includes that State and an authority of that State;).

¹¹⁶ *ITAA* s 23F(1) (definition of 'employee' included director as an employee of a company, irrespective of whether or not the relationship of master and servant existed between him and the company).
At general law, a director is not an employee of a company - see *Normandy v Ind. Coope & Co Ltd* (1908) 1 Ch 84, 104; *Re Lee, Behrens & Co Ltd* (1932) 2 Ch 46, 48; *Hutton v West Cork Railway Co* 23 Ch D 654, 672. A director acting in a dual capacity - ie a managing director or a governing director, may be an employee - see *Lee v Lee's Air Farming Ltd* (1960) 3 WLR 758, 769; *Lincoln Mills (Aust) Ltd v Gough* (1964) VR 193, 197-198.

¹¹⁷ The former *ITAA* s 23F(1) (definition of 'dependant' included the spouse and any child of the employee).

¹¹⁸ *ITAA* s 23F(2).

¹¹⁹ *ITAA* ss 23F(16), (17).

¹²⁰ *ITAA* s 23F(18).

¹²¹ A superannuation fund had to comply with certain public securities investment requirements before 30 June 1985.
ITAA div 9B - Superannuation Funds, ss 121B-121E, as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961. The 30/20 rule was included in this Division in ss 121C(1)-(12), effective from 1 March 1961. Later amended by *Income Tax Laws Amendment Act 1981*, No 108 1981.

compulsory investment in public securities. This compulsory investment was known as ‘the 30/20 rule’.¹²² It was abolished on 11 September 1984 with effect from the commencement of that year of income.¹²³

Any employer could establish a superannuation fund for employees, governed by a trust deed or rules and vested in a trustee. The employer could also be the trustee¹²⁴.

If a fund did not, in a particular year, satisfy all these requirements, the Commissioner had a discretionary power to apply the section if the trustee of a fund satisfied him that, because of special circumstances, it would be reasonable to do so.¹²⁵

If a s 23F fund failed to qualify for exemption from income tax because the trustee failed to comply with specific requirements, then it may have been eligible for tax relief if it complied with the

ITAA s 121C(1), as inserted by Income Tax and Social Services Contribution Assessment Act (No 3) 1964, No 3 1964, repealed by Taxation Laws Amendment Act 1985, No 49 1985.

The validity of the insertion of Division 9B was challenged in *Fairfax v FC of T* [1965] 14 ATD 135 as being a law not with respect to taxation but promoting investment in public securities. It was held that the enactment was valid.

This section only applied to ss 23F and 23(ja) funds.

From 1 July 1985, compliance with the in-house asset rules applied.

A new s 121C was inserted by *Taxation Laws Amendment Act (No 2) 1985, No 123 1985*, first applicable to assessments for the year of income commencing 1 July 1985. Later repealed by *Taxation Laws Amendment Act (No 4) 1987, No 138 1987*.

This section only applied to ss 23F and 23FB funds.

¹²² See [3.3.1].

¹²³ Ibid.

¹²⁴ *ITAA s 6(1)* (definition of ‘trustee’ was:

in addition to every person appointed or constituted trustee by act of parties, by order, or declaration of a court, or by operation of law, includes –

- (a) an executor or administrator, guardian, committee, receiver, or liquidator; and
- (b) every person having or taking upon himself the administration or control of income affected by express or implied trust, or acting in any fiduciary capacity, or having the possession, control or management of the income of a person under any legal or other disability).

¹²⁵ *ITAA ss 23F(7), 121C(4)*.

provisions of s 79.¹²⁶ See Chapter 5 - 'Other Superannuation Funds'.

4.3.2 Requirements for exemption by Section 23F Superannuation Funds

As previously stated, the recommendations of the Committee fell into two categories. The first related to the protection of the Federal Government's revenue and the second related to the protection of members' entitlements. The requirements in s 23F superannuation funds also related to these two categories. The provisions for the protection of the members' entitlements included that the trustee:

- ensured that the fund was an indefinitely continuing fund¹²⁷ established and maintained solely to provide superannuation benefits for either or both:
 - (i) employees in the event of their retirement or in other circumstances approved by the Commissioner¹²⁸; and
 - (ii) their dependants in the event of the employee's death¹²⁹;
- in each year of income received contributions from the employer for each employee who had a right to receive benefits from the fund;¹³⁰

¹²⁶ ITAA s 79 (voluntary contributions to pension funds), as inserted by *Income Tax Assessment Act 1944*, No 3 1944, as repealed by and new provisions inserted by *Income Tax Assessment Act 1965*, No 103 1965. Later repealed by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984 as from 1 July 1984 and replaced by s 23FB, as inserted by the same Act.

¹²⁷ An indefinitely continuing fund is a fund that will not be terminated or be wound up after a specified period.

¹²⁸ ITAA s 23F(2)(a)(i).

¹²⁹ ITAA s 23F(2)(a)(ii).

The original s 23F(2)(a), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964 did not include 'either or both of' in reference to the implementation of paragraphs (i) and (ii). This meant that it was necessary for a fund to comply with both sub-paragraphs. The alteration to include this phrase inserted by *Income Tax Assessment Act 1965*, No 103 1965 ensured that there was no doubt that a fund might be established and maintained to provide benefits on retirement of an employee or for dependants on the death of an employee or to provide benefits in either or both of these circumstances.

¹³⁰ ITAA s 23F(2)(b). In the original and substituted provisions of s 23F, an employer was required to contribute to a fund in each year of income for the benefit of each of his employees who had a right to receive benefits. PIB No 8, 2 explained that '...it will be

-
- fully secured the rights of employees and their dependants eligible to receive benefits from the fund;¹³¹
 - defined the rights and gave written notice of the existence of those contingent rights promptly to each member/employee;¹³²
 - applied forfeited benefits or rights to the provision of benefits or additional benefits for other employees and their dependants on a reasonable basis.¹³³

Whilst compliance with the other requirements of s 23F was essential to establish the exempt status of the income of a superannuation fund, these requirements directly related to the protection of the Federal Government's revenue and indirectly to protection of members' entitlement by preserving the tax exempt status of the fund. These included that the trustee:

- was not authorised by the fund to accept contributions from any parties other than specified parties;¹³⁴
- ensured that the benefits being provided by the fund for any employee were reasonable¹³⁵, having regard to such matters as salary, period of service, the benefits being provided by other employees' funds of a kind qualifying for exemption

sufficient if each employer, having one or more employees who are members of the fund, contributes to the fund during the year of income for the benefit of one or more (but not necessarily all) of his employees who are members of the fund.'

¹³¹ ITAA s 23F(2)(d).

¹³² ITAA s 23F(2)(e). In the original and the substituted s 23F, the right to benefits under the fund had to be notified in writing to each member. This was modified to notification of the existence of the right to benefits as inserted by *Income Tax Assessment Act 1973*, No 51 1973.

¹³³ ITAA s 23F(2)(f), (g).

¹³⁴ ITAA s 23F(2)(c). A specified party was the employee; an employer of the employee; a company in which an employer of the employee has a controlling interest; or if an employer of the employee was a company - a person who was associated with that company. ITAA s 23F(1) expanded the definition of 'person' to include a partnership.

¹³⁵ The Commissioner applied the standards of reasonableness determined for the purposes of s 23F in stipulating the maximum deduction allowed for contributions to a fund by an employer under s 82AAE. The standard of reasonableness were increased at various times. The Commissioner was given the power to allow the deduction of a greater amount if there were special circumstances justifying such greater deduction.

and other factors considered relevant by the Commissioner;¹³⁶

- ensured that the amount in the fund was not substantially in excess of the amount that was necessary for providing benefits that employees and their dependants had rights to receive at present and in the future.¹³⁷

These requirements were administrative. The Commissioner's investigation was usually necessary for detection of non-compliance. The Commissioner cited breaches of these requirements where appropriate and the requirement to 'fully secure' the employees' rights to support arguments that a trustee was not maintaining a fund solely to provide for employees' retirement.¹³⁸ The trustees of a fund could seek the Commissioner's approval for variation of the application of a requirement or his discretion to interpret circumstances as appropriate for compliance.¹³⁹

The requirements of *ITAA* s 121C before 30 June 1985¹⁴⁰ included statutory rules dictating minimum levels of investment in 'public securities'¹⁴¹. Consequently, this limited the level of investment by a superannuation fund for employees in the contributing employer.

¹³⁶ *ITAA* s 23F(2)(h).

¹³⁷ *ITAA* s 23F(2)(i).

¹³⁸ *Case C49 71 ATC 225; Case W 100 89 ATC 813; Case 25/93 93 ATC 314.*

¹³⁹ *ITAA* s 23F(7).

¹⁴⁰ *ITAA* s 121C was repealed on 11 September 1985.

¹⁴¹ *ITAA* s 6(1) (definition of 'public securities' to mean:

- (a) Commonwealth securities;
- (b) bonds, debentures, stock or other securities issued by a State, Territory, municipal corporation, local governing body or public authority set up under a Commonwealth, State or Territory law;
- (c) securities issued in respect of a loan to a company whose principal business is the supply and distribution in the Commonwealth of gas, water or electricity by a system of reticulation but did not include
- (d) securities referred to in paragraph (b) not being securities to which paragraph (e) applies) issued in respect of a loan raised outside Australia and the Territories unless there is in force a declaration by the Treasurer, published in the Gazette that those securities shall be public securities for the purposes of this Act; or
- (e) securities issued after 12 April 1976 by a bank).

These rules were known as the 30/20 public securities investment rule. Broadly, a fund's assets should have included 'public securities' costing not less than 30% of the total assets cost and that those securities included 'Commonwealth securities'¹⁴² costing not less than 20% of the total assets cost. The original inclusion of *ITAA* s 121C was a protection of the Federal Government's revenue to ensure funding of the infrastructure.¹⁴³

The in-house asset rule replaced the 30/20 public securities investment rule.¹⁴⁴ The in-house asset rule limited the proportion of the fund's assets that could be lent to or invested in the sponsoring employer or an associate of such an employer.¹⁴⁵ The basic rule required that at all times during the income year the cost of the 'in-house assets' of a superannuation fund for employees should not exceed 10% of the cost of all the assets of the fund.¹⁴⁶ The application of the rules varied according to whether the fund was established before 12 March 1985 or on or after that date.¹⁴⁷ In-house assets of a fund were those assets that

¹⁴² *ITAA* s 6(1) (definition of 'Commonwealth securities' to mean bonds, debentures, stock or other securities issued under an Act, but does not include –

(a) securities (not being securities to which paragraph (b) applies) issued in respect of a loan raised outside Australia unless there is in force a declaration by the Treasurer, published in the Gazette, that those securities shall be Commonwealth securities for the purposes of this Act; or

(b) securities issued after 12 April 1976 by a bank).

¹⁴³ The Treasurer, the Rt Hon Harold Holt MP, 'Income Tax and Social Services Contribution Assessment Bill 1961', (Second Reading Speech delivered at the House of Representatives, Canberra).

¹⁴⁴ *ITAA* s 121C, as inserted by *Taxation Laws Amendment Act (No 2) 1985*, No 123 1985 first applicable to assessments for the year of income commencing 1 July 1985.

¹⁴⁵ *ITAA* ss 121C(4), (5).

¹⁴⁶ *ITAA* s 121C(18) provided for funds that commenced or ceased during the year. The rules only applied for that part of the year the fund was in existence.

¹⁴⁷ For funds established after 11 March 1985, the basic 10% rule first applied for the 1985/86 year of income. The restriction should have been complied with at all times during the income year – s 121C(4).

For funds established before 12 March 1985, s 121C(5) provided that the 10% limit was phased-in over a 10 year period so that the funds could meet the limit by natural growth rather than by mandatory repayment of loan-backs to the employer sponsor. The rule for these funds over the phasing-in period from 1 July 1985 to 30 June 1995 was that the cost of the fund's in-house assets must not exceed at any time during the relevant income year the greater of:

consisted of loans to or investments¹⁴⁸ in an employer-sponsor¹⁴⁹ or an associate¹⁵⁰ of an employer-sponsor. The in-house asset rule in the *ITAA* was included as protection of members' entitlements in the event of the failure of the employer's business.¹⁵¹

The consequence of non-compliance with the 30/20 rule on investment of assets and the subsequent in-house asset rule was the imposition of tax at rates declared by the Parliament¹⁵²

In 1964, taxation of dividends from private companies and income from non-arm's length transaction was introduced, subject to the Commissioner not approving this income as acceptable for exempt

- the cost of the in-house assets held as at 11 March 1985 but must not exceed 70% of the cost of all assets of the fund at that date; and
- 10% of the cost of all the assets of the fund - s 121C(5)(a), (6).

The concessional treatment of funds existing on 11 March 1985 continued until the end of the income year commencing 1 July 1994. For the year commencing 1 July 1995 and later years, the 10% limit was applied to all funds regardless of when they were established - ss 121C(4), (5)(b).

¹⁴⁸ *ITAA* s 121C(1) (definition of 'investment' was any mode of application of money for the purpose of gaining interest, income or profit).

¹⁴⁹ *ITAA* s 121C(2)(a), an employer who contributed to a superannuation fund for the benefit of an employee (including a director) or dependants of an employee was treated as an employer-sponsor of the fund.

ITAA s 121(2)(b), a company controlled by the employer and which contributed to the fund was also treated as an employer-sponsor.

Where the employer was a company, any person connected with the employer company and who contributed was connected with a corporate employer where:

- the person has a controlling interest in the employer;
- the person was a company in which the controlling interest was held by a person who had a controlling interest in the employer; or
- the person was the beneficial owner of shares in the employer - s 121C(3).

¹⁵⁰ *ITAA* s 121C(1) referred to s 26AAB for the definition of 'associate'. In broad terms, in *ITAA* s 26AAB(14) any person who, by reason of business or family connections, was regarded as being associated with a particular person.

¹⁵¹ A concern shared by:

1. Taxation Review Committee, Commonwealth Government of Australia, *Full Report* (1975) 'Asprey Report' [21.101];
2. Committee of Inquiry, Commonwealth Government of Australia, *Occupational Superannuation in Australia* (1977) 'Hancock Report Part Two' 104 [7.13];
3. Committee of Enquiry, Commonwealth Government of Australia, *Australian Financial System* (1981) 'Campbell Report' 349 [20.126];
4. Commonwealth Taskforce, *Occupational Superannuation* (Parliamentary Paper No 27, Parliamentary Library, Commonwealth Government of Australia, 1983) 'Task Force Report' 36 [4.30].

¹⁵² Rates applied: *Income Tax Act 1936 to 1975*; *Income Tax (Companies and Superannuation Funds) Act 1976 to 1985*; *Income Tax Rates Act 1986*.

treatment. This measure was introduced to protect the Federal Government's Revenue as well as preventing circumvention of the rules for the current benefit of some or all members as well as ensuring the protection of the interests for retirement of all members.

See Chapter 3 for details of application of the 30/20 Rule¹⁵³ and In-house Rule.¹⁵⁴ Also in Chapter 3 are the taxation consequences of receiving dividends from private companies and not dealing at arms' length in relation to transactions.¹⁵⁵

4.3.3 Challenges of application of section 23F by the Commissioner

Whilst the trustee of a superannuation fund had to comply with a number of tests to the satisfaction of the Commissioner for s 23F funds, the main issues relating to the members' benefits that emerged as lacking clarity and requiring interpretation by the Boards of Review/courts were:

- the circumstances which determined if a fund was established for the benefit of employees or their dependants or for some other purpose¹⁵⁶;
- the circumstances which determined if a fund was maintained solely for the benefit of employees or their dependants¹⁵⁷ or for some other purpose;
- the meaning of 'fully secured' in the context of employees benefits being fully secured in a superannuation fund¹⁵⁸; and
- what matters did the Commissioner take into account when exercising his discretionary power and factors that influenced his opinion.

¹⁵³ Chapter 3 [3.3.1].

¹⁵⁴ Chapter 3 [3.3.2].

¹⁵⁵ Chapter 3 [3.3.3].

¹⁵⁶ ITAA s 23F(2)(a).

¹⁵⁷ Ibid.

¹⁵⁸ ITAA s 23F(2)(d).

The Commissioner provided advice on his interpretation of the application of specific requirements in Public Information Bulletins ('PIB')¹⁵⁹ Nos 6 and 8.

4.3.3.1 *Funds to be established for benefit of employees or their dependants*

As discussed previously in relation to s 23(j)(i) fund, the intention and establishment of a fund for benefits of employees for their retirement or their dependants on their death are pivotal initial steps of providing the protection of the members' entitlements.

The courts established some of the principles that applied when determining if a fund had been established for the benefit of employees or their dependants when they decided disputes relating to funds established under *ITAA* s 23(j)(i). The principles established in these cases also applied to and were cited in cases relating to s 23F funds. The principles established were:

1. an intention of the creator of the trust to create a superannuation fund;¹⁶⁰
2. documentation of the objectives and purpose of the superannuation fund;¹⁶¹
3. language and definitions in the documentation support the objectives and purpose of superannuation;¹⁶²
4. evidence of the initial property establishing the superannuation fund to be held on trust;¹⁶³
5. creation of membership of the superannuation fund by allocation of contributions to a member's benefit account¹⁶⁴.

¹⁵⁹ PIBs replaced the informal method of communication from the Commissioner. The ATO produced PIBs in Volumes 1 (1965) to 8 (1966).

¹⁶⁰ *Mahoney v FC of T* (1965) 13 ATD 519; *Compton v Commissioner of Taxation* (1966) 39 ALJR 400.

¹⁶¹ Ibid.

¹⁶² *Associated Provident Funds Pty Ltd v FC of T* (1966) 14 ATD 333.

¹⁶³ *Mahoney v FC of T* (1965) 13 ATD 519; *Associated Provident Funds Pty Ltd v FC of T* (1966) 14 ATD 333.

The Commissioner clarified his interpretation of *ITAA* s 23F in PIB No 6. He advised that ‘other circumstances approved by the Commissioner’ quoted in s 23F(2)(a)(i) would generally include assistance provided in the event of sickness, injury or other misfortunes. He advised that some provisions for certain payments included in a trust deed could be merely classified as ‘incidental to the operation of a superannuation fund’ and would not, except in very rare circumstances, constitute a breach of paragraph (a) ie being established and maintained for the sole purpose of providing retirement benefits for employees. He also advised that it was not his opinion that providing both benefits, providing superannuation benefits to employees in the event of their retirement and their dependants in the event of the death of the employees, was required to satisfy the purpose test.

The Commissioner provided his interpretation of what constituted an ‘indefinitely continuing fund’.

Funds that are to be conducted for a relatively few years and then distributed will not generally satisfy the ‘indefinitely continuing’ test.¹⁶⁵

4.3.3.2 *Funds maintained solely for benefits of employees or their dependants*

The introduction of the requirement in *ITAA* s 23F for a fund to be maintained as a superannuation fund solely for the benefit of employees was one of the integral methods adopted to protect members’ benefits.¹⁶⁶ This coupled with the application of the 30/20 rule, the in-house asset rule and the taxing of ‘special

¹⁶⁴ *Mahoney v FC of T* (1965) 13 ATD 519; *Compton v Commissioner of Taxation* (1966) 39 ALJR 400.

¹⁶⁵ PIB No 6, Office of the Commissioner of Taxation, Canberra, May 1965, 6.

¹⁶⁶ The consensus of opinions of the Justices in the cases relating to s 23(j)(i) indicated that for a trust to be established as a superannuation fund for the benefit of employees, the deed must document this specific purpose and no other.

income' restricted the investment in the contributing employer and the potential and inherent risk to members' benefits. The restricted investment of the fund for the benefit of employees protected the integrity of the fund and was a method adopted for protecting the members' entitlements.

The establishment of a fund for the benefit of employees or their dependants was not enough to qualify the claimant for exemption of its income from income tax. The Judges in some of the cases before the courts considered that for a fund to be entitled to exemption from income tax under the provisions of s 23(j)(i), it should be maintained solely for the benefit of employees or their dependants.¹⁶⁷ Funds established under the later *ITAA* s 23F were expressly required to be 'maintained solely' for the provision of benefits for employees or their dependants.

This question of a fund being 'maintained solely' for the provision of benefits for employees or their dependants was a pertinent question the Commissioner addressed when assessing a claim for exemption from income tax by a fund. 'Solely' and 'benefit for employees or their dependents', as opposed to benefit for some other party eg the employer, required interpretation.

The principles that were developed in the cases relating to s 23(j)(i) indicating that a superannuation fund was not being applied for the benefit of employees were if:

- benefits were being applied to others rather than employees;¹⁶⁸
- benefits were for a restricted class of employees;¹⁶⁹

¹⁶⁷ *Mahoney v Federal Commissioner of Taxation* 14 ATD 519; *Compton v Federal Commissioner of Taxation (No 2)* 14 ATD 295.

¹⁶⁸ *Mahoney v Commissioner of Taxation* (1965) 39 ALJR 62, 63; *Associated Provident Fund v FC of T* (1966) 14 ATD 333, 351.

¹⁶⁹ *Driclad Pty Ltd v Commissioner of Taxation* (1966) 121 CLR 45.

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- the money earned did not result from the investment of contributions;¹⁷⁰
 - the motivation of the investment strategy was to earn profits in a tax free environment¹⁷¹.

The following cases involving s 23F funds adopted these same principles. The term ‘solely’ was interpreted both narrowly and with a more liberal approach.

In *Case C49*¹⁷², the income of the s 23F fund did not qualify for exemption from income tax because the fund failed to satisfy s 23F(2)(a).¹⁷³ The trustee of the fund had not maintained it solely for the provision of superannuation benefits for employees in the event of their retirement or their dependants in the event of their death. The evidence showed that the fund provided ‘a convenient medium’ through which land transactions took place. Transactions were funded by large mainly interest-free loans by the employer and by a related superannuation fund. At a later date, the superannuation fund sold a freehold property built for resale by the fund to the trustee (the sole beneficiary and only employee) on interest free and extended terms, providing the employee with substantial benefits long before normal retirement age. Taken into account when deciding against the taxpayer and confirming the Commissioner’s decision and his assessment was the fact that the taxpayer had not obtained approval from the Commissioner for the fund’s provision of benefits in any other circumstances in terms of

¹⁷⁰ *Mahoney v FC of T* (1965) 13 ATD 519; *Compton v FC of T* (1966) 14 ATD 295; *Associated Provident Fund v FC of T* (1966) 14 ATD 333.

¹⁷¹ *Associated Provident Fund v FC of T* (1966) 14 ATD 333.

¹⁷² 71 ATC 225.

¹⁷³ The Commissioner also considered that the benefits were excessive in reaching his decision – *ITAA s 23F(2)(h)(iv)*. The Board of Review agreed with this decision.

s 23F(2)(a)(i), ie the provision of benefits before retirement in the form in which they emerged.¹⁷⁴

This case demonstrated that a superannuation fund's ability to fund transactions by interest free loans and the ability of members to withdraw their entitlement prior to their retirement in a form which was to the detriment of the fund and providing a benefit to the member prior to retirement did not conform with the Federal Government's policy encouraging people to save for their retirement. Non-compliance with the requirement to maintain a superannuation fund solely for the benefit of employees puts a member's benefits at risk.

In similar circumstances in *Case L13*¹⁷⁵, the Board of Review accepted the submission made by the Commissioner, that the fund did not satisfy the provisions of s 23F(2)(a), ie it was not a fund established and maintained solely to provide superannuation benefit on the taxpayers' retirement.¹⁷⁶

In contrast, the AAT in *Case X60*¹⁷⁷ held that a superannuation fund that made a number of loans on which it did not collect interest nevertheless satisfied the sole purpose test of s 23F(2)(a). The AAT considered the principles established in *Driclad Pty Ltd v*

¹⁷⁴ It was the practice of the ATO to require that trust deeds not permit trustees to make payment of benefits otherwise than in cash other than the transfer of life assurance policies. Taxation Ruling IT 2027, issued on 22 March 1983, changed this practice and stated that there would be no objection to the payment of superannuation benefits otherwise than in cash where the relevant trust deed contained the appropriate provisions.

¹⁷⁵ 79 ATC 72.

¹⁷⁶ The Commissioner also submitted that, if the fund did not satisfy the provisions of paragraph 23F(2)(a), it did not satisfy the provisions of paragraph 23F(2)(h). The Board stated that as the provisions of paragraph 23F(2)(a) were not satisfied, it was unnecessary to proceed further in the question of whether a fund had been established and the exemption provisions applied.

Case L13 79 A.T.C. 72, 75 [13] cited Windeyer J in *Scott v FC of T* (1966) 40 ALJR 265, 278; Kitto J in *Compton v FC of T* (1966) 116 CLR 233, 244.

¹⁷⁷ 90 ATC 438.

*FC of T*¹⁷⁸ in which the fund operated under the deed governing the fund and lent moneys of the fund at interest back to various companies of the Driclad group.¹⁷⁹ The AAT concluded that an incidental, but not purposeful, benefiting of someone other than the employees and their dependants by the trustee in the conduct of an investment program was not of itself a contravention of the sole purpose test. Mr Hogan of the AAT stated that this decision cannot be seen, of itself, as a contravention of the sole purpose test seen to arise under s 23(j)(i) in the decision in *Compton* and later enshrined in the statute by s 23F(2)(a). ...¹⁸⁰

In *Case W100*¹⁸¹, the AAT held that a superannuation fund was not established for the sole purpose of providing superannuation benefits for employees in the event of their retirement or for dependants of employees in the event of the death of the employees. Whilst the fund complied with the requirements of ss 23F(2) and 121C, it had a contingency fund with more than five times the amount of the sole member's entitlement necessary for providing benefits.¹⁸² It was found that there were no special circumstances that existed in relation to the fund during the years of income under review to make it reasonable for s 23F to have effect. The governing director ('the controlling mind of the group' of companies) was the sole member of the fund even though the trust deed provided for other employees to be members. Evidence established that there was no prospect of any other employee being

¹⁷⁸ (1966) 121 CLR 45: Barwick and Kitto JJ agreed with the principles established in *Compton v Federal Commissioner of Taxation* (1966) 14 ATD 295, 67.

¹⁷⁹ *Driclad Pty Ltd v Commissioner of Taxation* (1966) CLR 45, 62. The principle established was that if there was derogation of, or so as to defeat, the rights of employees in the fund as constituted, the conclusion would follow that the fund was not being applied for the purpose for which it was established. This established principle was cited and relied on in the following cases: *Raymor Contractors Pty Ltd* (1991) 91 ATC 4259; *Walstern Pty Ltd* (2003) ATC 5076.

¹⁸⁰ Ibid 446.

¹⁸¹ 89 ATC 813.

¹⁸² ITAA s 23F(2)(h).

admitted to membership of the fund and the contingency fund was held for the benefit of the governing director.

In *FC of T v Roche*¹⁸³, the Commissioner argued that the fund was not administered for the 'sole purpose' of providing superannuation benefits for employees. He contended that the overall operation of the fund provided the taxpayers with collateral tax advantages as well as low interest borrowings. Pincus J commented that a fund might be maintained for a purpose within s 23F, even if an important reason for its having been established and maintained was the obtaining of tax deductions.¹⁸⁴ His Honour disallowed the claim for exemption of the fund for the years in question because of non-compliance with the 30/20 rule.

The factors relevant for consideration as evidence of compliance with the sole purpose test for the establishment and maintenance of a s 23F superannuation fund that emerged from the challenges by the Commissioner were confirmed as those established in relation to s 23(j)(i) funds:

- the language and terms of the trust deed;
- any underlying or alternative motivation for establishing the superannuation fund established for the benefit of employees;
- the operations of the superannuation fund providing benefits to parties other than the employees on retirement; and
- the accruing of excessive members' benefits.

Where the courts found that there were reasons for the existence of a superannuation fund other than the purpose prescribed in the legislation, the superannuation fund could not be said to be

¹⁸³ 91 ATC 5024.

¹⁸⁴ View also expressed by Davies J, with whom Wilcox J agreed, in *Raynor Contractors Pty Ltd v FC of T* 91 ATC 4259, 4260-4261.

established and maintained for providing benefits for employees in the event of their retirement or their dependants in the event of their death. Income of such a fund should not be exempt from income tax.

Restricting the powers of investment of the trustee of a superannuation fund was a principle that developed from the decisions in the cases before the courts. They show that the courts found that provisions were substantively underlying the purpose of the legislation and reinforced the policy of protecting members' benefits. Adopting the principle minimized the risk related to members' benefits. The investment in and loans to the contributing employer or associates put members' entitlements at risk in the event of the business of the employer failing. Non-compliance with the terms of any loan agreement and non-performance of any investment reduced the earning capacity of the fund and the ultimate entitlement of the members.

4.3.3.3 Benefits of employees to be fully secured

After establishing that a superannuation fund was established and maintained solely for the benefit of employees or their dependents, the benefits for employees or their dependents had to be 'fully secured' for the superannuation fund for employees to be eligible for exemption from income tax. The requirement for benefits to be fully secured is paramount in ensuring that the members' entitlements are protected and available when they are required.

The meaning of 'fully secured' has different interpretations depending on its usage. For example, statute confers the rights to payment for long service leave. The law makes these rights 'fully secured' to employees. The employer cannot take them away from the employees. A loan facility is 'fully secured' when adequate

security, either real estate or financial instrument secures the repayment of the facility.

The term ‘fully secured’, as it related to the rights of employees to benefits within superannuation funds, required interpretation. A separate issue was whether these rights were ‘fully secured’ against the fund.

The early general provision *ITAA* s 23(j)(i) made no reference to a requirement for employees’ rights to be ‘fully secured’ for a fund to be eligible for exemption from income tax. In the counterpart section relating to the deductibility of contributions, s 66¹⁸⁵, the rights of employees had to be ‘fully secured’ for the Commissioner to allow the deduction.

When deliberating on the term ‘fully secured’ pre-*ITAA* in *Metropolitan Gas Co. v FC of T*¹⁸⁶, Gavan Duffy CJ and Starke J when considering the claim of a fund established by a public utility to be exempt, summarised the issue as follows:

The question which the Commissioner has to consider and upon which he must be satisfied, is whether the rights of the employees to receive the benefits, pensions or retiring allowance have been fully secured. It is not whether the stipulated rights have been

¹⁸⁵ *ITAA* s 66.

An employer was entitled to a tax deduction if the fund to which it ‘set apart or paid’ was ‘to provide individual personal benefits, pensions or retiring allowances for his employees as is proportionate, to the extent to which those employees ... engaged in producing assessable income of the taxpayer,’ ... where

(a) the taxpayer is under a legal obligation to set apart or pay that sum; and
(b) the rights of the employees to receive the benefits, pensions or retiring allowances are fully secured.

ITAA s 66(1) was as follows:

Where a taxpayer, for the purpose of making provision for individual personal benefits, pensions or retiring allowances for, or for dependants of, employees of the taxpayer, being or including employees engaged in producing his assessable income, sets apart or pays in the year of income a sum as or to a fund from which such benefits, pensions, or allowances are to be provided, and the rights of the employees or dependants to receive the benefits, pensions or allowances are fully secured, an amount ascertained in accordance with the provisions of this section shall be an allowable deduction.

ITAA s 66, as repealed by and *ITAA* s 82AAC, as inserted by *Income Tax and Social Service Contribution Assessment Act (No 3) 1964*.

¹⁸⁶ (1932) 47 CLR 621, 631. *Income Tax Assessment Act 1922-1929* s 23(1)(j).

secured in due legal form, but whether the Commissioner is satisfied that the actual receipt of the individual personal benefits, pensions and retiring allowances from the fund to which an employer has made contributions from his assessable income is fully secured. The Commissioner has a wide discretion: it is part of his function to satisfy himself that employees shall in fact get the benefits of the fund, that they are protected against unreasonable deprivation of benefits from the fund, that the management and investment of the fund are properly safeguarded, and so forth.

The deed establishing a fund defined the rights conferred upon employees and their dependants to receive benefits from a superannuation fund. Until a deed was executed, the rights of employees were not fully secured.¹⁸⁷ Also, the rights of employees to the benefits of a fund were not fully secured during the retrospective period where a deed was expressed to operate retrospectively.¹⁸⁸ The fact that contributions were ‘set apart’ and not paid did not detract from benefits being ‘fully secured’.¹⁸⁹

The trustee’s discretionary power within the deed was an issue that drew attention in the context of employee benefits being fully secured. Over many years, the courts established and legislation in the various States defined and refined the duties of a trustee¹⁹⁰

¹⁸⁷ *Case D25* (1953) 4 TBRD; *Case LI5* (1960) 11 TBRD; *Case NI8* (1963) 13 TBRD.

¹⁸⁸ *Danmark Pty Ltd v FC of T* (1944) 7 ATD 333; *Waddington v O’Callaghan* (1931) 16 TC 187; *Case D47* (1953) 4 TBRD.

¹⁸⁹ *Winchombe Carson Ltd v FC of T (NSW)* (1938) 5 ATD 69, 74; *Case F22* (1955) 6 TBRD.

¹⁹⁰ The duties of a trustee are:

1. to acquaint himself with the terms of the trust;
2. to get in the trust property;
3. not to impeach the validity of the trust instrument or the title of the cestuis que trust;
4. to adhere to and carry out the terms of the trust, subject to qualification;
5. to act impartially between the beneficiaries;
6. properly to invest the trust funds;
7. to keep and render proper accounts and to give full information when required;
8. to exercise reasonable care;
9. not to delegate his duties or powers;
10. to pay and transfer the trust property and the income thereof to the right persons;
11. to act gratuitously;

and a trustee with a discretionary power¹⁹¹ and the rights of a beneficiary^{192, 193} Remedies were available to injured parties for a trustee to make good any loss caused by breach of trust arising from negligent or wrongful dealings. However, the courts viewed the discretionary power of a trustee in a superannuation deed as detracting from the security of the employees' rights. This evolved because there was no qualification or restrictive provision within the *ITAA* for the holding of the position of trustee of a superannuation fund. An employer could be the trustee of a superannuation fund.

The discretionary power of a trustee with no restrictions relating to the investment of the superannuation fund detracted from the Federal Government's policy intent. There was a possibility of a conflict of interest of the trustee if the trustee was also the employer. A fund under discretionary control of the employer was not 'fully secured' and members' benefits were not protected.

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12. not to deal with the trust property for his own benefit, or otherwise to profit by the trust.

R.P. Meagher QC & W.M.C. Gummow, *Jacobs Law of Trusts in Australia*, Butterworths 5th ed, 1986 [1701]–[1736].

¹⁹¹ The duties of a trustee with a discretionary power are:

1. to act honestly and in good faith;
2. to act upon genuine consideration - 'the exercise of an active discretion' *Partridge v The Equity Trustees Executors and Agency Co Ltd* (1947) 75 CLR 149, 164;
3. to exercise his power with due consideration for the purpose for which it was conferred, and not for some ulterior purpose.

Ibid [1609].

¹⁹² The rights of a beneficiary are:

1. to possession of the trust property;
2. to compel performance of the trust;
3. to restrain a breach of trust;
4. to approach the court for determination of questions of construction and administration;
5. to extinguish the trust;
6. to follow the trust property;
7. to claim in persona against a third party who has received trust property.

Ibid [2301]–[2321].

¹⁹³ *Ibid* [380]–[456].

In *FC of T v The Northern Timber and Hardware Company Proprietary Limited*¹⁹⁴, Fullagar J of the Full High Court of Australia stated that a fund that the taxpayer had

under its unfettered control to deal with as it chose and to be unmade as it was made, viz, by a stroke of a pen ... would be a fund which provided the employees with no security of any sort.

Taylor J of the High Court of Australia also expressed this view in *Driclad Pty Ltd v FC of T*¹⁹⁵. If the fund remained, either directly or indirectly, under the employer's

control or within his disposition so that the rights of his employees and their dependants to receive the benefits provided by the scheme are liable to be defeated at his option,

the benefits were not 'fully secured'. His Honour also commented that he did not

think that the question whether the rights of members to receive the benefits provided are fully secured calls for an assessment of the stability of the investment which they had made.

It is not required for the fund to be secured, only the existence of the benefits.¹⁹⁶

In *Case A11*¹⁹⁷, the AAT confirmed the Commissioner's assessments on the ground, inter alia, that the fund was under the control of the permanent managing director of the employer and the rights of the participants to receive benefits were liable to be defeated at his option. The AAT also highlighted the managing director's conflict of interests as rendering the rights of participants as being not 'fully secured'.

¹⁹⁴ (1960) 103 CLR 650, 657.

¹⁹⁵ (1966) 121 CLR 45, 58-59.

¹⁹⁶ Ibid 60.

¹⁹⁷ 69 ATC 53, 58. Cited Taylor J's view in the *Driclad Pty Ltd v Commissioner of Taxation* (1966) 121 CLR 45.

In *Case U227*¹⁹⁸, CJ Bannon QC, Deputy President of the AAT referred to the law set out in the judgements of *The Northern Timber and Hardware Company Proprietary Limited case*¹⁹⁹ and *Driclad's case*²⁰⁰ and relied on the interpretation of 'fully secured' in those cases. It was found that

the rights of the members of the fund, or the claimed members, were not fully secured within the meaning of sec 23F(2)(d). ...The fund operated largely as a discretionary fund An important element in securing the rights of employees is informing them of their rights and this was not done.²⁰¹

In *Case X62*²⁰², however, it was held that the unfettered discretion of the trustee to deny access to information about the operation of the fund to any member of the fund did not affect the question of whether the fund was 'fully secured'. Mr M B Hogan of the AAT referred to and relied on *Driclad*²⁰³ and *Metropolitan Gas*²⁰⁴ for his decision, allowing the objection.

... having joined the scheme, employees have agreed to be bound by its provisions in relation to the determination of benefit, however restrictive those provisions may appear, and it is the benefit determined under these provisions that has to be seen upon consideration of the manner in which the fund is constituted 'to be fully secured'. ...

Referring to the decision of Taylor J in *Driclad*²⁰⁵, Mr Hogan relied on his Honour's observation that the rights being fully secured did not call for an assessment of the stability of the investments made by the trustee.

¹⁹⁸ 87 ATC 1265.

¹⁹⁹ (1960) 103 CLR 650.

²⁰⁰ (1966) 121 CLR 45.

²⁰¹ Ibid 1267.

²⁰² 90 ATC 469, 480.

²⁰³ (1966) 121 CLR 45, 58-59.

²⁰⁴ (1932) 47 CLR 621, 631.

²⁰⁵ (1966) 121 CLR 45, 60.

P M Roach, Senior Member of the AAT summarised pertinent questions relating to the security of members' rights in *Case X16*.²⁰⁶

'How could it be said that the rights of members were fully secured, when information was withheld from 'members' as to their status as members?' and, *a fortiori*, as to their entitlements to benefit. On the other hand, the question can also be rhetorically asked for the taxpayer: 'How can it be said that the rights of members were not fully secured when, subject to qualifying for benefit, the trustee could have no basis for resisting any claim to benefit?'²⁰⁷

It was further noted that

... it is not necessary to find that there must be an expectation on the part of either the employer or the employee, that each employee will actually come to qualify for benefit. It is sufficient that the employee will be entitled to benefit if as a member of the fund he satisfies the qualifying conditions.²⁰⁸

In summary, the cases cited above established the following principles. For a benefit to be 'fully secured' in a superannuation fund, an employee must have knowledge of the existence of the right to receive the benefits and an entitlement to receive the benefits, even if subject to qualifying conditions. The discretion of the trustee must not be a factor in determining whether the employee receives the benefit.

It follows that a 'fully secured' superannuation benefit for an employee is, by definition, a chose in action. 'It is a thing of which a person has not the present enjoyment, but merely a right to recover it (if withheld) by action.'²⁰⁹

²⁰⁶ 90 ATC 180.

²⁰⁷ Ibid 191.

²⁰⁸ Ibid.

²⁰⁹ E.R. Hardy Ivamy, *Mozley & Whiteley's Law Dictionary*, (Butterworth, 10th ed, 1988) 79.

4.3.3.4 *The Commissioner's discretion*

A general provision that allowed the Commissioner to exercise his discretionary power, *ITAA* s 23F(7), provided that a fund may be considered to have satisfied any requirement of s 23F(2) and claim exemption from income tax if:

the trustee of the fund satisfies the Commissioner that, by reason of special circumstances that existed in relation to the fund during that year of income, it would be reasonable for this section to have effect as if that requirement had been complied with.²¹⁰

A reference to the Board of Review/AAT could include, in addition to other grounds supporting the claim, a request for relief from non-compliance with *ITAA* s 23F(2) by application of s 23F(7) for the Commissioner's discretionary power and the 'special circumstances' of the case in question.²¹¹ In PIB No 6, it appeared that all the circumstances listed as being applicable to s 23F(2)(b)²¹² were regarded by the Commissioner as constituting special circumstances within the meaning of s 23F(7) and that the words 'special circumstances' would be treated by the Commissioner in a somewhat liberal manner. What constituted 'special circumstances' outside this list was the issue the Board of Review/AAT needed to address.

In *Case W82*²¹³, the AAT accepted that 'special circumstances' should not be narrowly construed but failed to expand the interpretation. In *Case W109*²¹⁴, consideration of 'special circumstances' was assessed within the circumstances

²¹⁰ *ITTA* s 23F(6), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964.

²¹¹ *Case 25/93* 93 ATC 314 - contributions within the fund were excessive within s 23F(2)(h); *Case W109* 89 ATC 859 - notice of entitlement not given to employees other than principal within s 23F(2)(e); *Case W82* 89 ATC 722 - benefits provided were 'excessive in amount' as provided by s 23F(2)(h).

²¹² See below n 230.

²¹³ 89 ATC 722 730.

²¹⁴ 89 ATC 859 867.

surrounding the claim. In this case, it was held that the circumstances were not ‘special’ when considered within the overall context of the claim. In *Case A69*²¹⁵, ‘special circumstances’ warranting consideration by the Commissioner to exercise his discretion under s 23F(7) to overlook non-compliance with s 23F(2)(h) did not arise because the excessive benefits being provided for a fund member resulted from the member’s very large initial contribution.

PIB No 6 acknowledged that an inadvertent failure to meet one of the tests could result in a fund not being eligible for exemption for up to two years if discovery of the defect occurred when the Commissioner examined the return of income. However, it stated that:

inadvertent failures to comply with particular tests will be met by exercise of the discretionary power in favour of a fund that has not knowingly withheld relevant information and which corrects the deficiency as soon as is reasonably practicable.²¹⁶

4.3.4 *Advice by the Commissioner about the application of s 23F*

The Commissioner’s advice in PIBs was a guide to his interpretation of the provisions in the *ITAA*. The need to provide this information became apparent when the income tax law changed in 1964.

4.3.4.1 *Notice in writing*

PIB No 6 indicated that there was not any precise way in which the notification of the existence of the rights to benefits²¹⁷ should be given to a member. Satisfactory ways were to include:

²¹⁵ 69 ATC 385.

²¹⁶ PIB No 6, 4-5.

²¹⁷ *ITAA* s 23F(2)(e).

the giving of a copy of the rules (or an extract therefrom) showing the benefits to be received or how they may be calculated, the distribution to all members of a reasonable summary of the rules governing the benefits or, in the case of future members, the inclusion on a form of application for membership of a reasonable summary of the rights to benefits.²¹⁸

The affirmative action of the employer defining and advising employees of their rights within the fund was interpreted as evidence of the intention of an employer to maintain a superannuation fund for the benefit of employees or their dependants. It was established in decisions made by the Authorities that an integral part of rights being ‘fully secured’ was the notice in writing of the rights to the employees. The discovery of non-compliance with this requirement was dependant on the Commissioner’s investigation of a fund, usually as a result of the disallowance of a claim.

In *Case U227*²¹⁹, the absence of written notice, together with other evidence, supported an argument by the Commissioner ‘that the rights of the members of the fund, or the claimed members, were not fully secured within the meaning of sec. 23F(2)(d)’²²⁰.

In *Case W109*²²¹, it was held that the fund did not at any time constitute a fund to which s 23F applied because the trustee had not notified by the required date the employees of the company, other than the taxpayers, of their rights as defined by the terms and conditions applicable to the fund.

²¹⁸ PIB No 6, 11.

²¹⁹ 87 ATC 1265.

²²⁰ *Case U227* 87 ATC 1265.

²²¹ 89 ATC 859.

However, in *FC of T v Roche*²²², Pincus J stated that ‘it is inconceivable that the Tribunal would regard the absence of written notice ... as destructive of the exemption from tax which s 23F creates ...’. From this statement, it could be argued that the non-compliance with this requirement for notice in writing to the members of their rights within the fund by itself was not sufficient for the Commissioner to disallow a claim by a fund for exemption from income tax. This was contrary to the view of PM Roach, Senior Member of the AAT in *Case W109* mentioned above.

4.3.4.2 *The Commissioner’s general discretionary power*

The inclusion of the Commissioner’s discretionary power in the new legislation in the *ITAA* for superannuation funds in 1964 created concern and confusion about the application of this power. Its inclusion was to provide a means to correct any inadequacies and anomalies of the provisions as they related to a particular taxpayer or to allow extraordinary circumstances for a fund to be taken into account. It allowed the Commissioner to implement the Federal Government’s policy for saving for retirement and to ensure that the spirit of the legislation was complied with. Because of the broad purpose of the provisions that included this reference, they lacked clarity.

Emphasising the concern of the tax paying public, the ATO received numerous questions about the application of the provisions. PIB No 1 outlined some common questions asked on how the discretionary powers would be exercised. They included:

- What matters will the Commissioner consider relevant?
- How can a taxpayer or his adviser know what these matters are?
- When should an application for the exercise of a discretion be made?

²²² 91 ATC 5024, 5030.

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- What information will the Commissioner require?
 - Will a detailed application have to be made each year?
 - Is there a right of appeal against a decision of the Commissioner on an application?
 - Will the Commissioner personally cope with all his new discretionary powers or will he delegate them to numerous members of his staff?
 - How can uniformity in the exercise of the discretionary powers be achieved?

These questions demonstrated that there was a need for direction on the application by the Commissioner of the provisions in the *ITAA*.

Initial guidelines²²³ and later income tax rulings²²⁴, restricting the application of the Commissioner's discretionary power to within certain parameters, provided an indication of his intention when exercising his discretion.

The provisions in s 23F that contained the Commissioner's discretionary power that created the most concern were:

- the requirement provisions for:
 - forfeited benefits;
 - excessive benefits;
 - exemption of private company dividends;
 - exemption of income from transactions not at arm's length;
 - the general provision for the Commissioner to allow compliance with the regulations 'in special circumstances', and
- the assessment provisions for:
 - the 30/20 rule; and

²²³ Before March 1965, the Commissioner issued memoranda from Head Office relating to new or previously advised interpretations of the taxation law.

²²⁴ The Taxation Ruling system was introduced as from 1 December 1982 as a method of disseminating decisions on interpretation of the laws administered by the Commissioner of Taxation.

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- the in-house asset rule.

The initiative for having the discretionary power exercised lay with the trustees of a fund. The trustees may have preferred that the fund be dealt with under some other provisions of the law and not cause the Commissioner to exercise his discretionary powers.

Except for the issue of dealing with forfeited benefits, the discretionary power of the Commissioner related directly to the protection of the Federal Government's revenue. If the Commissioner chose not to exercise his discretion, the fund would not be eligible to apply the exemption provisions.

(a) Forfeited benefits

Provisions of the *ITAA* regulated the application of benefits for employees whose rights had ceased.²²⁵ The application of benefits for purposes other than for the employee for whom they were initially intended was potentially open to abuse. For example, these benefits could have been distributed to the principals of the employer. To restrict such practice, these provisions included discretionary references – ‘...approved by the Commissioner, ... having regard to all the circumstances’, ‘for ... any other purposes approved by the Commissioner’ and ‘... reasonable, having regard to all the circumstances’.

In PIB No 6, the Commissioner indicated that he would approve the application of lost or forfeited benefits relating to paragraph (ii)²²⁶

²²⁵ *ITAA* s 23F(2)(f) related to allocated funds and *ITAA* s 23F(2)(g) related to unallocated funds.

²²⁶ PIB No 6, 13. Application of lost or forfeited benefits were:

- (a) welfare benefits to assist employees in the event of financial hardship, sickness, accident or other misfortune causing hardship;
- (b) supplementary benefits for retired members of the fund provided that the total benefits are not regarded as being excessive within para. (h);

of s 23F(2)(f) provided that ‘reasonable benefits’ levels were adhered to and were not, in the Commissioner’s opinion excessive in terms of s 23F(2)(h).²²⁷ For paragraph (iii) of s 23F(2)(f), PIB No 6 also elaborated on application of lost or forfeited benefits.²²⁸ Similar application of lost or forfeited benefits were available for s 23F(2)(g).²²⁹

4.3.4.3 Annual contributions

Section 23F(2)(b) did not include any reference to the discretionary power of the Commissioner to waive the requirement to contribute to a fund during the year of income by an employer in respect of each employee. However, in PIB No 6, the Commissioner listed eleven instances²³⁰, where, provided that there were no other circumstances against the application of s 23F, he would exercise

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- (c) additional benefits for members still employed if the application is made equally among the members on a *pro rata* basis among all the members or among members on the basis of economic needs.
- 227 Ibid 13-15.
- 228 Ibid 13:
- (a) payment of administration expenses of the fund;
 - (b) payment of an employee’s contribution to relieve hardship or in special circumstances;
 - (c) payment to an employer to recompense him for defalcations, etc. of the employee or for losses due to misconduct of the employee;
 - (d) payment to an employer in circumstances that resulted in the payment being assessable income of the employer.
- 229 Ibid 14.
- 230 PIB No 6, 7-8.
- 1. The contribution is made by an associated enterprise and not by the employer;
 - 2. A member for whom a contribution was made in earlier years has changed his employment and contributions for his benefit by his former employer have ceased;
 - 3. Moneys provided by the trustees out of accumulations in earlier years or lost or forfeited benefits make it unnecessary for the employer to contribute;
 - 4. An employee is absent from duty;
 - 5. An employee remains in employment beyond the normal retiring date but contributions by the employer cease;
 - 6. Past contributions by the employer and (in most cases) the employee, together with income and capital gains in the fund, are sufficient to provide the proposed benefits;
 - 7. Further contributions would result in the fund losing tax exemption through the application of paras. (h) or (i);
 - 8. An employee is serving a reasonable qualifying period before the employer is required to contribute;
 - 9. Contributions by way of life assurance premiums are unnecessary while an employee is disabled;
 - 10. A fund is conducted on an actuarial basis and contributions are made only when actuarially necessary;
 - 11. The financial position of an employer makes it inappropriate for him to contribute.

his discretionary power to waive compliance with 23F(2)(b). He also stated that the list did not:

necessarily encompass all circumstances in which the discretionary power will be exercised to overcome a failure to meet the test prescribed in paragraph (b). Additional circumstances will doubtless be presented as grounds for the exercise of the discretion and all cases will be carefully considered.²³¹

The requirement for contributions for employees in the provisions of the *ITAA* did not discriminate between full-time, part-time and casual employees.²³² This imprecision in the application of this requirement allowed interpretation by employers either to obtain a maximum deduction for employees who may not be entitled to receive benefits eg casual employees, or to discriminate against employees because of their employment status, eg part-time employees.

4.3.5 *Inadequacies*

Section 23F attempted to clarify the legislation that applied the intention of the Federal Government's policy to provide tax incentives to employers to contribute to superannuation funds. It attempted to provide provisions for compliance to protect members' entitlement by:

- the superannuation fund being an indefinitely continuing fund established and maintained solely for the benefit of employee in their retirement and their dependants on the employee's death;²³³

²³¹ PIB No 6, 8.

²³² Taxation ruling IT 294 [11] provided the guideline that associated persons whose weekly hours of employment are 30 hours or more would be regarded as a full-time employee. Where an employee, either at arm's length or associated, was employed for less than 10 hours a week it was a question in each case, depending upon the nature and value of the services rendered, whether any deduction for superannuation contributions was warranted.

²³³ *ITAA* ss 23F(2)(a), (b).

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- making the benefits fully secured;²³⁴
 - making the members aware of the existence of the fund and their entitlements;²³⁵
 - applying rules for application of a member's benefits on cessation of his rights;²³⁶
 - applying rules about contributions²³⁷.

The imposition of investing requirements, also enhanced the protection of members' benefits.

These amendments to the legislation addressed some of the issues required to protect members' benefits and the Federal Government's revenue but some issues requiring interpretation remained outstanding.

4.3.5.1 *Inadequacies established by the Commissioner*

The issues in *ITAA* s 23F identified as remaining inadequate for the protection of members' benefits and the Federal Government's revenue within the legislation, which led to interpretation and clarification by Rulings and the courts and amendments in the *ITAA*, included:

- the employer, or a related party, lending funds, often interest free, to the superannuation fund that then earned income that was exempt from income tax²³⁸;
- the employer, or a related party, making contributions to the superannuation fund to obtain a tax deduction for the contributions and the superannuation fund then participating in one or all of the following:

²³⁴ *ITAA* s 23F(d).

²³⁵ *ITAA* s 23F(e).

²³⁶ *ITAA* ss 23F(2)(f), (g).

²³⁷ *ITAA* ss 23F(c), (h), (i).

²³⁸ *Associated Provident Funds Pty Limited v FC of T* (1966) 14 ATD 333; *Case C49 71* ATC 225; *Case U174 87* ATC 998.

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- (i) lending the contributions back to the employer, or a related party, often interest free. This strategy provided a deduction to the employer for contributions. If interest was charged/paid, there was a further deduction for the employer and interest paid/accrued to the superannuation fund was exempt.²³⁹ Ultimately, the loan back may have been forgiven with existing members' rights to benefits ceasing or distributions may have been made from the fund to members still in employment²⁴⁰;
 - (ii) purchasing shares in the contributing employer, or a related party, providing capital back to the company and subsequently a means of distributing profits to the superannuation fund that were exempt from income tax²⁴¹;
 - (iii) not advising employees of the existence of their rights to benefits nor defining the rights of individual employees so that any claim for the rights would be unlikely²⁴²;
 - (iv) terminating employees before they became eligible for any entitlement of benefits so that when the trustee wound up the fund the only employees remaining to receive benefits of the fund were parties related to the employer²⁴³;
 - the superannuation fund borrowing money and purchasing shares with this money in the contributing employer or a

²³⁹ *Case L13 79 ATC 72; FC of T v Roche 91 ATC 5024.*

²⁴⁰ Taxation Ruling IT 2067 [31] announced that this practice could result in the exemption previously granted to the fund and deductions for contributions allowed to the employer being re-examined. It may be concluded that the fund had not at all times since its inception been maintained solely for the purposes of providing superannuation benefits.

²⁴¹ *Associated Provident Funds Pty Limited v FC of T* (1966) 14 ATD 333; *Compton v Commissioner of Taxation* (1965) 39 ALJR 400; *Case B15 70 ATC 61*; *Driclad Pty Ltd v Commissioner of Taxation* (1966) 121 CLR 45.

²⁴² *Case U227 87 ATC 1265*; *Case W109 89 ATC 859*; *Case X16 90 ATC 180*; *FC of T v Roche 91 ATC 5024.*

²⁴³ *Raymor Contractors v FC of T* 90 ATC 4684; *Bayton Cleaning Company Pty Limited v FC of T* 91 ATC 4076.

- related party, providing capital to the company and a means of distributing profits which were exempt from income tax²⁴⁴;
- the employer, or a related party, making excess contributions to the superannuation fund to obtain a greater tax deduction and/or accumulating amounts in the superannuation fund in excess of the provisions required to provide benefits for employees. This excess accumulation of funds led to a further tax benefit in that the excess funds earned additional income that was exempt from tax²⁴⁵;
 - the employer, or related party, making ‘catch-up’ contributions for persons close to retirement²⁴⁶.

To minimise the use of loan back arrangements, the Commissioner announced that from 1 July 1982 these loans had to carry a minimum commercial rate of interest specified by the Taxation Office.²⁴⁷ Any calculation of superannuation contributions had to take the earnings on the loan back into account at the higher of the specified rate and the rate actually paid.²⁴⁸ The Commissioner tempered the announcement advising that where the trustee was absolutely free in the choice of investments, the investment in the employer would not constitute a loan back.²⁴⁹

There were no accounting and reporting provisions for superannuation funds within the provisions of the *ITAA*. From 1 July 1982, an independent auditor²⁵⁰ was required, every year in

²⁴⁴ *Compton v Commissioner of Taxation* (1965-66) 39 ALJR 400.

²⁴⁵ *Case A69 69 ATC 385*.

²⁴⁶ *Case W82 89 ATC 722*.

²⁴⁷ Taxation Ruling IT 294 [31]-[35]. Further explanations were provided in Taxation Ruling IT 2067 [23]-[31].

²⁴⁸ *Ibid* [32].

²⁴⁹ Taxation Ruling IT 2067 [24]. For example, the trustee investing some portion of the moneys in a fund in shares of the employer, the employer being a larger public company; where the trustee acquired real property and leased it to the employer or associated entity at a commercial rental.

²⁵⁰ Taxation Ruling IT 294 [47], Taxation Ruling IT 2067 [37]. The auditor need not be a registered company auditor. Membership of either the Institute of Chartered Accountants

the case of a loan back fund, and every three years in the case of other funds, to provide a certificate verifying that the assets of the fund:

- actually existed in the fund;
- were in a form suitable for the purpose for which they existed, ie that in the event of retirement or resignation of employees, the assets were readily realisable; and
- indicating whether, in the opinion of the auditor, the fund was being conducted in accordance with its constituent document.²⁵¹

4.4 Section 23(jaa) Superannuation Funds

The funds for the provision of superannuation benefits for employees of government or other public authorities were referred to as public sector plans and related to employees of –

- the Australian government;
- the government of a State or Territory;
- a local government body;
- a public authority; or
- a university.

From 1936, *ITAA s 23(j)(i)* included exemption from income tax income of public sector plans. Public sector plans were excluded by definition from the requirement to comply with the 30/20 rule.²⁵²

In 1964, *ITAA s 23(jaa)* replaced this general exemption.²⁵³ It allowed exemption from tax for the income of a provident, benefit,

in Australia or the Australian Society of Accountants was sufficient qualification for the purpose of auditing a fund and supplying a compliance certificate.

²⁵¹ Taxation Ruling IT 294 [46]–[47].

²⁵² *ITAA s 121B* (definition of ‘superannuation fund’, as inserted by *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961).

²⁵³ *ITAA s 23(jaa)*, as inserted by amendment *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, Date of Assent, commencement 23 November 1964.

superannuation or retirement fund established by an Act, a State Act or an Ordinance of a Territory, or a local government body or by other public authorities established by similar means.

The exemption from income tax for public sector funds was unqualified. *ITAA s 23(jaa)* referred to the establishing of a fund for the public sector but did not refer to the on-going maintenance or management of the fund. There was no specific requirement for the fund to remain a fund for the public sector nor was there any penalty tax if the body breached their governing Act or Ordinance. The exemption of income from tax did not depend on the nature of the fund's investments.²⁵⁴

A number of public sector superannuation plans operated on an unfunded basis. This meant that these plans paid benefits on an emerging cost basis, often from consolidated revenue and did not receive regular contributions for the provision of benefits. Because there was no 'fund', these schemes were not subject to tax.

The plans for the employees of State, Territory or local government all had their own special features. Similarly plans for employees of public authorities and universities related to the circumstances of their employment.

The rationale behind the unqualified exemption of public sector funds provided by s 23(jaa) was that government controlled the fund, either directly, where an Act or Ordinance established the fund, or indirectly, where the relevant body or authority was constituted by an Act or Ordinance. It was expected that the fund

²⁵⁴ *ITAA s 121C(1A)*, as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. Reference in this section was to those funds that the section applied to. *ITAA s 23(jaa)* was not included.

would be established and operate on a basis that could be considered reasonable.

From 1 July 1988, all superannuation funds, including public sector funds were subject to tax. Up to 30 June 1990, they were classified as complying superannuation funds and qualified for concessional treatment.

In response to Reports from a number of Committees to the Federal Government, from 1 July 1990 public sector funds were required to satisfy all the relevant standards and conditions imposed under the *OSSA* if they were to continue to be classified as complying superannuation funds. See Chapter 6 for analysis of the provisions and regulations for compliance by public sector fund relating to the requirements of *OSSA* and *OSSR*.

4.5 Conclusion

The introduction of the provisions relating to the exemption of income from income tax in new expanded legislation in *ITAA s 23F* replacing the original generic provision of *ITAA s 23(j)(i)* provided some clarity to the application for compliance. Its introduction as recommended by the Ligertwood Committee was in response to the abuse of the original provision in an attempt to protect the Revenue. This Committee did not recommend any amendment to funds established for self-employed persons as it found that there was no evidence of abuse.

Over the years, a number of different funds to which tax concessions applied developed to provide opportunities for all persons to save for their retirement. These and funds established for self-employed persons are discussed in Chapter 5.

It has been shown in the challenges by the Commissioner in the court and before the Board of Review that there were inadequacies in *ITAA s 23F* which made members' benefits vulnerable. These inadequacies led to the Federal Government appointing a number of committees to ascertain the anomalies, inconsistencies, unnecessary complexities and other similar defects in the legislation, how the legislation operated and to formulate proposals to remedy the defects. Chapter 6 discusses the results of the reports to the Federal Government made by these committees. It reviews the rationale for the need for new legislation and its implementation, taking into account the inadequacies identified by the courts and the Commissioner in his advices to taxpayers and their advisers.

CHAPTER 5

REGULATION

OTHER SUPERANNUATION FUNDS

Chapter 2 set out the background to superannuation regulation and defined critical terms. Chapter 3 detailed the exempt and concessional tax treatment of superannuation funds, this being the incentive provided by the Federal Government to encourage people to save for their retirement. It showed that this strategy was successful.

Chapter 4 showed that superannuation funds for employees had been central to government policy and its development. It focused on regulation governing superannuation funds for employees of both the private and public sectors during the period 1936 to 1986.

This Chapter addresses the other superannuation funds that were developed to cater for non-employees and for those employees whose employers did not provide superannuation benefits. These funds were developed to encourage saving for the retirement of individuals.

The main types of superannuation funds developed during the period 1936 to 1986 for non-employees regulated by the ITAA were:

1. seeking exemption from income tax:
 - (i) self-employed funds - s 23(ja)¹;
 - (ii) life assurance company superannuation funds - s 110².

¹ ITAA s 23(ja), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1952*, No 90 1952, Date of assent, commencement 18 November 1952, amended by *Income Tax Assessment Act 1965*, No 103 1965, *Income Tax Laws Amendment Act 1981* No 108 1981, as repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

² ITAA div 8 ss 110 - 116D regulation of the taxation of superannuation funds controlled by Life Assurance Companies, amended by *Income Tax Assessment Act 1942*, No 22 1942, *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961, *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, *Income Tax Assessment Act 1973*, No 51 1973, *Statute Law Revision Act 1973-1974*, No 216

- (iii) foreign superannuation funds - s 23(jb)³;
 - (iv) approved deposit funds - s 23FA⁴; and
2. seeking tax relief because of non-compliance - superannuation funds for employees and self-employed funds - s 79⁵. Section 23FB replaced s 79 in 1984.⁶

This Chapter examines each of these superannuation funds during the period 1936 to the introduction of *Occupational Superannuation Standards Act* ('OSSA'). The provisions for each type of superannuation fund are complex. In some cases, interpretation was dependent on guidelines issued by the Commissioner. For the purpose of this analysis, the distinguishing terms and conditions are discussed to highlight the diversity of superannuation funds available for saving at concessional tax rates and of the provisions regulating them.

By developing different types of superannuation funds to assist different categories of persons and by offering tax incentives, the Federal Government confirmed its policy of encouraging people to save for their retirement. This Chapter will demonstrate the

³ 1973, *Income Tax Assessment Act (No 2)* 1974, No 126 1974, *Income Tax Assessment Act* 1975, No 80 1975, *Income Tax Laws Amendment Act 1981*, No 108 1981.

⁴ From 1 July 1968, *ITAA* s 6(1) included a definition of what constituted a 'foreign superannuation fund'. *ITAA* s 23(jb), as inserted by *Income Tax Assessment Act (No 4)* 1967 No 5 1967, effective from 1 January 1968.

⁵ *ITAA* s 23FA, as inserted by *Income Tax Assessment Amendment At (No 3)* 1984, No 47 1984, applicable to assessments for the year of income commencing 1 July 1983, as repealed by *Taxation Laws Amendment Act (No 4)* 1987, No 138 of 1987, as replaced by *ITAA* s 23FD by *Taxation Laws Amendment Act (No 4)* 1987, No 138 of 1987 first applicable to assessments for the year of income commencing 1 July 1986. Part of superannuation benefits, inter alia payments on termination, became liable to tax effective from 1/7/83 – *ITAA* ss 27A-27J.

⁶ *ITAA* s 79 original section repealed, substituted s 79, as inserted by *Income Tax and Social Services Act (No 3)* 1964, No 110 1964, further substituted by s 79, as inserted *Income Tax Assessment Act* 1965, No 103 1965, later amended by *Income Tax Assessment Act*, No 51 1973, *Income Tax Laws Amendment Act 1981*, No 108 1981, as repealed by *Income Tax Assessment Amendment Act (No 3)* 1984, No 47 1984.

⁶ *ITAA* s 23FB, as inserted by *Income Tax Assessment Amendment Act (No 3)* 1984, No 47 1984, applicable to assessments for the year of income commencing 1 July 1984.

commencement of the implementation of mechanisms to protect members' benefits.

5.1 Self-employed Persons' Superannuation Funds

Before 1952, income of non-employee superannuation funds was not exempt from income tax. Superannuation funds established for self-employed persons were initially trusts and taxed under the provisions relating to trusts.⁷ This was a disincentive for non-employees to save for retirement and was regarded as inequitable when compared with the tax incentives provided to encourage employers to provide retirement benefits for employees.

The Federal Government acknowledged the need to encourage self-employed persons to establish pension funds. The Commonwealth Committee of Taxation⁸ recommended that the most appropriate method of achieving this was to allow the income of these types of funds the same tax exemption that applied to the income of employees' pension funds. The Federal Government adopted this principle and extended the application of these tax incentives to the superannuation funds established for the contributions of self-employed persons.⁹

This exemption of the income of self-employed superannuation funds from income tax was introduced in 1952 to remedy inequities.¹⁰ A deduction for contributions made by self-employed

⁷ ITAA pt III div 6.

⁸ Commonwealth Committee on Taxation, Commonwealth of Australia, *Report on Income Tax – concessional allowances for life insurance premiums, superannuation fund contributions, Friendly Society dues and like payments (Reference No 9)* (1951).

⁹ The Treasurer Sir Arthur Fadden, 'Income Tax and Social Services Contribution Assessment Bill (No 3) 1952' (Second Reading Speech delivered at the House of Representatives, Canberra, 18 September 1952).
ITAA s 23(ja), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1952*, No 90 1952, Date of Assent, commencement 18 November 1952.

¹⁰ The Treasurer Sir Arthur Fadden, 'Income Tax and Social Services Contribution Assessment Bill (No 3) 1952' (Second Reading Speech' delivered at the House of Representatives Canberra, 18 September 1952).

persons was not allowed until 1980.¹¹ Prior to this time, limited concessional deductions were allowed.¹² The announcement of this new superannuation arrangement relating to the deduction of contributions by self-employed persons was made in the 1980 Federal Budget.¹³ The stated intent behind the amendments was:

... to extend to such people (self-employed persons or employees who are not supported by an employer sponsored scheme), where no other contributions are made on their behalf a taxation benefit broadly comparable to the 'matching employer' contribution of supported employees.¹⁴

It was considered to be a 'significant incentive to encourage people who [did] not have the support of an independently funded superannuation scheme to make better provision for their retirement'.¹⁵

At the time of the introduction of the exemption for superannuation funds established for self-employed persons, there were relatively few funds in existence and there were no clear guidelines as to the basis on which the funds were to be

¹¹ ITAA pt III div 3 sub-div AB ss 82AAS, 82AAT, as inserted by *Income Tax Assessment Act (No 4) 1980*, No 124 1980. Deductions were allowable for contributions made by eligible persons to an eligible superannuation fund after 19 August 1980. Discussed by Commonwealth Committee on Taxation, Commonwealth Government of Australia, *Report of the Commonwealth Committee on Taxation* (1961), 'Ligertwood Report' 150-1 [723]-[729]; Taxation Review Committee, Commonwealth Government of Australia, *Full Report* (1975), 'Asprey Report'. [21.105], [21.114]; Occupational Superannuation In Australia, Final Report of the National Superannuation Committee of Inquiry, Part II March 1977, The Acting Commonwealth Government Printer Canberra 1977. Parliamentary Paper No 70/1977, ('Hancock Report') xiii-xiv; 113-5 [7.41]-[7.45].

¹² ITAA s 82H allowed a limited deduction for payments combined with premiums for life policies. ITAA s 82H(1)(b)(i), as inserted by *Income Tax and Social Services Contribution Assessment Act 1950*, No 48 1950; ITAA s 82H(1G), as inserted by *Income Tax Assessment Act 1973*, No 51 1973; as repealed by *Income Tax Assessment Act (No 2) 1975*, No 117 1975 but continued to apply until 30 June 1975. From 1 January 1973, ITAA ss 159N, 159R(8), as inserted by *Income Tax Assessment Act (No 2) 1975*, No 117 1975 for superannuation funds compliant with the requirements of ITAA ss 23(jaa). (ja) 23F or 79, commenced on 1 July 1973.

¹³ Recommended by the Committee of Inquiry, Commonwealth Government of Australia, *Occupational Superannuation in Australia* (1977), 113 [7.42].

¹⁴ The Treasurer, the Rt Hon John Winston Howard, '1980 Federal Budget' (Speech delivered at the House of Representatives, Canberra, 12 August 1980).

¹⁵ The Treasurer, the Hon John Howard, 'Income Tax Assessment Amendment Bill (No 4) 1980' (Second Reading Speech delivered at the House of Representatives, Canberra).

conducted. It was decided that it was undesirable for conditions to be imposed with precise terms. Such conditions may prove to be unduly restrictive, especially for funds already in existence which may be affected. As a result of this decision, the exemption was subject to broad rules. It was also stated that it might be necessary to review the conditions in the light of practical experience.¹⁶

5.1.1 **Requirements for exemption from tax**

ITAA s 23(ja)¹⁷ exempted from tax the income of a provident, benefit, superannuation or retirement fund for 'classes of persons who are eligible for membership' provided the fund complied with specified requirements. It specified that its application referred to a fund 'not being a fund established for the benefit of employees'. As in the case of superannuation funds for employees, it was intended to exempt the types of funds established for the benefit of groups of persons, e.g. self-employed¹⁸ members of a profession.

To qualify, the fund must have:

- had no less than 20 eligible persons at any one time entitled to receive present or future benefits from the fund, other than as a spouse, child or dependant of a member¹⁹;
- had its applicable terms and conditions approved by the Commissioner. Conditions taken into consideration by the Commissioner included:
 - (i) satisfactory terms of the regulatory rules governing the fund and its operation;
 - (ii) the class of persons eligible for membership;
 - (iii) the reasonableness of the benefits;

¹⁶ Explanatory Notes to the *Income Tax and Social Services Contribution Assessment Bill (No 3) 1952*.

¹⁷ See above n 1.

¹⁸ Explanatory Notes to the *Income Tax and Social Services Contribution Assessment Bill (No 3) 1952*.

¹⁹ ITAA s 23(ja)(i), as amended by *Income Tax Assessment Act 1965*, No 103 1965 to ensure that a wife or child of a member is always treated as a dependant of the member for the purposes of s 23(ja).

- (iv) the amount of the fund in relation to the benefits; and
- (v) such other matters as he may consider relevant.²⁰

The section required that a fund satisfied all the specified requirements.

The Commissioner set out guidelines for the approval of superannuation funds under section 23(ja).²¹ These included a restriction on the maximum permissible benefit and a limitation on the maximum contribution which a member may make in any one year, the limit being age related.²²

From 1961, a s 23(ja) fund had to comply with the 30/20 rule.²³ The ratio of public securities under the 30/20 rule had to be maintained at all times during the year if the fund was not to be taxable on its investment income, although the Commissioner had a discretion to exempt a fund from compliance in certain circumstances.²⁴ Where a fund was not exempt because of failure to comply with this rule, the investment income²⁵ was liable to be taxed.²⁶ The provisions requiring compliance with the 30/20 rule were abolished on 11 September 1984²⁷ with effect from the commencement of that year of income.²⁸

ITAA s 23(ja) was omitted and the requirements for self-managed superannuation funds were included in *ITAA* s 23FC in 1987.²⁹

²⁰ *ITAA* s 23(ja)(ii).

²¹ The Asprey Report [21.39].

²² Ibid.

²³ *ITAA* s 121C(1A)(a).

²⁴ *ITAA* ss 121C(4), (5).

²⁵ *ITAA* s 121B of *ITAA* defined 'investment income' to mean:
 assessable income, other than contributions to the fund, calculated as if the trustee of the fund were a taxpayer in respect of that income, being a resident, less all amounts that would be allowable deductions (other than the concessional deductions in respect of benefits) if that income were assessable income.

²⁶ *ITAA* s 121D. Rates applied: *Income Tax Act 1936 to 1975; Income Tax (Companies and Superannuation Funds) Act 1976 to 1985*.

²⁷ Repealed by *Taxation Laws Amendment Act 1985*, No 49 1985.

²⁸ Technically, this meant that most funds would qualify for exemption from tax on their investment income without having to satisfy the 30/20 rule at any time during 1984/85.

²⁹ *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

This coincided with the introduction of the *OSSA*.³⁰ The replacement section included the requirement for self-managed superannuation funds to comply with the provisions relating to dividends paid by private companies and income from non-arm's length transactions. This income for s 23(ja) superannuation funds was assessable only where it was derived after 29 October 1987.³¹

Chapter 3 discusses the requirements of the 30/20 Rule³², the application of the requirements relating to 'special income' and the tax consequences of non-compliance.³³

5.1.2 Advice by the Commissioner

The provisions of the *ITAA* for the taxation of s 23(ja) funds were imprecise and general in their language. To assist taxpayers and their advisers to interpret the generality of the section and anticipate the acceptable application of the provisions relating to the taxation of superannuation funds, the Commissioner published guidelines and later Rulings.³⁴

As a matter of practice, the Commissioner insisted on strict adherence at all times to guidelines that he set, although his discretionary powers to approve funds of this kind were wide. Guidelines issued by the Commissioner regarding the operation of s 23(ja) funds to qualify for exemption included the requirements that:

- the trustee of a fund accept contributions to the fund only from its members, who at the time of making the contribution to the fund, qualified as a self-employed person;³⁵

³⁰ *Occupational Superannuation Standards Act 1987*, No 97 1987.

³¹ *ITAA* s 23FC(2)(a).

³² Chapter 3 [3.3.1].

³³ Chapter 3 [3.3.3].

³⁴ See above n 21. PIB No 6; IT 2189; IT 2201; IT 2335.

³⁵ 'Self-employed' was not defined in the *ITAA*.

- annual contributions made by the member to all funds of which he was a member must not exceed a predetermined limit based on the age of the member;³⁶
- ‘reasonable’ maximum benefits ultimately to be provided must be restricted to amounts outlined in guidelines issued;³⁷
- in addition to the maximum benefit, the benefits generally should not be paid to a member before age 60³⁸ but they must be paid by age 70;³⁹ and
- unsecured loans to members and secured loans other than in prescribed circumstances⁴⁰ were generally prohibited.

In *Case G10 75 ATC 33*, the taxpayer owned and managed a block of flats. The Commissioner challenged the concept of what was self-employed. The taxpayer was not an employee and was not self employed in any occupation. There was nothing he could retire from on account of age or illness when he might be said to be ‘superannuated’. The Board of Review addressed what was the basis for a business. They found that evidence for the existence of a business were the elements of repetition and continuity of acts and transactions. By carrying on a business, a person could qualify as a self-employed person.

³⁶ Limitation set by and at the Commissioner’s discretion. PIB No 6, 19 effective date 1 July 1965. The Commissioner increased these limits when necessary to reflect changes in economic conditions. Taxation Ruling IT 2201 [16]-[30], effective date 1 July 1985.

³⁷ Limitation set by and at the Commissioner’s discretion. PIB No 6, 17 effective date 1 July 1965. This PIB stated that the scale of ‘reasonable benefits’ set out in the PIB for s 23F would apply for the purposes of s 23(ja), subject to special factors and as far as the circumstances would permit. The Commissioner increased these limits when necessary to reflect changes in economic conditions.

Taxation Ruling IT 2201 [13] effective date 1 July 1985. For employee of s 23F funds, a lump sum pre-tax benefit of 7 times final ‘notional salary’ at normal retirement age was permitted.

For non-employees of ss 23FB, 23(ja), a ‘notional salary’ for calculation of benefits was the average of the member’s net business income from all sources in the year of becoming entitled to benefits and the two previous years. ‘Net business income’ for superannuation purposes was generally the gross business income less allowable income tax deductions directly attributable thereto including prior year losses. In calculating net business income, rents, dividends and interest should generally be excluded. Where in a particular year the member incurred a loss from his business activities the ‘income’ of that year should be taken as nil.

³⁸ For a male member, the benefit was not payable before age 65 unless the person had completed 10 years’ membership.

³⁹ ATO Guideline: The Hancock Report 14 [2.28]; 21 [2.53].

⁴⁰ ATO Guideline: CCH Australia Limited, *Tax Library*, 1996 [8-120].

The trustees could lend money to a member who produced adequate security for the loan, where the loan was granted on normal commercial terms.

For other loan requests, the trustees required statements from the member in support of his application. These loans could be granted only where the trustees were satisfied that the member had been unable to obtain a loan from normal borrowing sources and that he would be in serious financial difficulties if a loan were not granted from the fund. The

5.1.3 Challenges by the Commissioner

Challenges by the Commissioner were related to whether contributions complied with the requirements for allowable deductions and not whether the superannuation fund was compliant for exemption of its income from tax.

5.1.4 Inadequacies established by the Government

In the Ligertwood Report, it was stated that, because exemption of s 23(ja) funds depended on the terms and conditions being acceptable to the Commissioner of Taxation, the Commissioner had effective control of these funds and no abuses had been brought to the attention of the Committee.⁴¹

In the Hancock Report, the disincentives for self-employed persons providing superannuation benefits for themselves were identified as:

1. the provisions of the *ITAA* constrained them (with few exceptions) to use s 79 funds whose income is only partially exempt from tax; and
2. the limited rebatable contributions⁴².

5.1.5 Alternatives

From 1965, if the trustee of a superannuation fund could not comply with the requirements of s 23(ja), eg did not have the minimum number of members, the trustee could establish a superannuation fund to comply with the requirements of *ITAA* s 79.⁴³ The trustee would invest assets of this fund in income-

amount of the loan must not exceed the total of his contributions to the fund up to that time.

⁴¹ Ligertwood Report 134 [738].

⁴² The Hancock Report 113 [7.41].

⁴³ See [5.2], [5.3]. *ITAA* s 23FB funds that replaced *ITAA* s 79 funds offered alternative opportunities for self-employed persons.

producing securities and obtain an annual deduction equal to 5% of the non-life policy assets cost to offset the income.⁴⁴

Alternatively, an eligible person could invest in a superannuation policy with a Life Assurance Company and achieve exemption from income tax. From 1961, changes to the *ITAA* exempted from tax that part of the investment income attributable to policies issued for the purposes of tax-exempt superannuation funds.⁴⁵ This exemption was subject to certain conditions, including compliance by the life assurance company with the 30/20 ratio in respect of all its assets.⁴⁶

A further option for a self-employed person was for her/him to incorporate her/his business to take advantage of the tax incentives available to employers. The Commissioner also gave professional persons the right to incorporate their practices if they wished to take advantage of the tax incentives available to employer-sponsored superannuation funds provided their professional bodies or associations allowed such incorporation.⁴⁷ Where a professional body or association did not allow incorporation,⁴⁸ structures were established to isolate fees from the profession, and a company was incorporated to carry on the remaining business to take advantage of the tax incentives.

5.2 Section 79 Funds

A type of superannuation fund, known as a s 79 superannuation fund, was introduced to cater for non-

⁴⁴ See [5.2.1] the requirements for tax relief of *ITAA* s 79 superannuation funds.

⁴⁵ See [5.5] on Life Assurance Companies.

⁴⁶ *ITAA* s 110A(4).

⁴⁷ Taxation Ruling IT 25: Incorporation of medical practices. Other professional taxpayers seeking approval of incorporation referred the matter to the ATO for consideration. The tax advantages of incorporation were restricted to superannuation contributions. Income splitting or income deferral methods were not allowed. The company had to distribute all net income to the professional shareholders of the company as salaries within the year of income that it was earned. There was also to be no limitation to professional liability.

⁴⁸ The Pharmacy Guild of Australia.

compliant superannuation funds.⁴⁹ The introduction of s 79 superannuation funds coincided with the introduction of s 23F superannuation funds, funds established for the benefit of employees. They provided an alternative to ss 23F, 23(jaa) and 23(ja) funds for saving for retirement. These funds received a tax benefit if they complied with the requirements of the *ITAA*.

The original *ITAA* s 79 relating to taxation of superannuation funds introduced in 1964 was repealed and a new *ITAA* s 79 was substituted in 1965.⁵⁰ Similar reasons as applied to the substitution of *ITAA* 23F relating to the discretionary power of the Commissioner and the right of appeal were cited for this substituted section.⁵¹

The substituted *ITAA* s 79 is the basis of this discussion. Reference to differences in the original *ITAA* s 79 are commented on in the footnotes if significant.

Section 79 superannuation funds were introduced by the Federal Government to encourage saving for retirement by those who could not or did not wish to comply with the provisions which allowed exemption of income from income tax.

Until 30 June 1984, a s 23F or s 23(ja) superannuation fund that was not exempt because it did not comply with any requirement for exemption was assessed on the superannuation fund's investment income at a non-concessional rate of tax.⁵² To avoid the imposition of this tax, the trustee of a superannuation fund could seek

⁴⁹ See above n 5.

⁵⁰ *Income Tax Assessment Act 1965*, No 103 1965.

⁵¹ See Chapter 4 [4.3].

⁵² *Income Tax Act 1936 to 1975; Income Tax (Companies and Superannuation Funds) Act 1976 to 1985*.

approval from the Commissioner for the fund to have tax relief under *ITAA* s 79.

ITAA s 79 superannuation funds were liable for tax on their investment income but allowed a special deduction equal to 5% of the cost, subject to adjustments, of their assets. For employers who could not, or did not wish to, comply with the requirement of the 30/20 rule for *ITAA* s 23F funds, *ITAA* s 79 allowed them to contribute to a superannuation fund obtaining a tax benefit and providing superannuation benefits for their employees or their dependants. *ITAA* s 79 also provided self-employed persons who could not, or did not wish to, comply with the requirements of the self-employed fund, in particular the requirement for a minimum fund membership of 20 persons, the opportunity to save for their retirement and obtain a tax benefit.

5.2.1 Requirements for tax relief

A superannuation fund seeking tax relief under the provisions of s 79 of *ITAA* had to satisfy some specific tests to qualify for relief.⁵³

The requirements were:

- the superannuation fund had:
 - to be an indefinitely continuing fund; and
 - to be maintained solely for the provision of superannuation benefits for members in the event of their retirement or in other circumstances approved by the Commissioner, or for dependants in the event of the death of the member;⁵⁴
- the rights of members to benefits were fully secured⁵⁵ and advised to the member at or before the time the first contribution was made on behalf of that member;⁵⁶

⁵³ *ITAA* s 79(2).

⁵⁴ *ITAA* s 79(2)(a).

⁵⁵ *ITAA* s 79(2)(b).

⁵⁶ *ITAA* s 79(2)(c).

- at all times the terms and conditions of the fund required that benefits be paid or commenced to be paid not earlier than the member's 60th birthday (except in the case of death, sickness or permanent incapacity for work) ⁵⁷ and not later than the 70th birthday. Lump sum benefits also had to be fully paid by the later of those dates⁵⁸;
- the terms and conditions of the fund were approved by the Commissioner having regard to whether:
 - the benefits being provided in respect of each member were reasonable;⁵⁹ and
 - the amount in the fund was not excessive with respect to the amount of benefits to be provided⁶⁰.

These tests corresponded to many of those applicable to qualifying employees' funds, the most pertinent being:

- the purpose and nature of the fund⁶¹;
- the requirement that benefits be fully secured and be notified to the members⁶².

The differences between qualifying employees' funds and s 79 funds were:

- persons who were gainfully occupied otherwise than as employees may be members of a s 79 superannuation fund;
- employers need not contribute for the benefit of employee members of a s 79 superannuation fund;
- there was no express restriction on the class of persons who may contribute for the benefits of a member of a s 79 superannuation fund;
- certain age limits were specifically prescribed.

⁵⁷ ITAA s 79(2)(f)(i).

⁵⁸ ITAA ss 79(2)(f)(ii)-(iii); s 79(11).

⁵⁹ ITAA s 79(2)(g).

⁶⁰ ITAA s 79(2)(h).

⁶¹ ITAA ss 79(2)(a)(i), (ii).

⁶² ITAA ss 79 (2)(b)-(c).

Similar conditions to those of s 23F and s 23(ja) funds applied to the application of forfeited benefits and for a trustee's undertaking in this regard.⁶³

The Commissioner had to approve a fund qualifying under these various tests.⁶⁴ He would not approve a fund if the benefits being provided by it were excessive, having regard to the Commissioner's scale of reasonable benefits and the benefits being provided for a member from any other s 79 fund or from any exempt fund.⁶⁵

The Commissioner did not have a discretion to ignore a failure of a s 79 superannuation fund to meet the requirements specified.

Neither the provisions for the requirements of a s 79 fund nor the assessing provisions of superannuation funds required that s 79 funds invest any part of their assets in any particular way or that investments comply with the 30/20 public securities investment rule. A s 79 superannuation fund had to comply with the assessing provisions relating to dividends from private companies and non-arm's length transactions.⁶⁶

5.2.2 Clarification by the Commissioner

Qualification for membership of a s 79 superannuation fund was not defined in that section of the *ITAA*. Amongst the requirements for compliance by a s 79 superannuation fund was that s 79 would apply only if benefits were to be provided to members on retirement 'from any business, trade, profession, vocation, calling, occupation or employment'.⁶⁷ It followed that persons whose only income was as a beneficiary of a trust or from investments were to be excluded. The Commissioner's view was that membership was for those

⁶³ *ITAA* s 79(2)(d)-(e).

⁶⁴ *ITAA* s 79(2)(g).

⁶⁵ *ITAA* s 79(2)(g). These exempt funds specifically include ss 23(ja), 23(jaa), 23F funds.

⁶⁶ *ITAA* s 121BA(2)-(5).

⁶⁷ *ITAA* s 79(2)(a)(i).

persons gainfully employed, ie an individual must be in gainful employment so as to be capable of retiring from it.⁶⁸ A fund would not be approved if it was not structured for membership by gainfully employed persons only. The term ‘gainfully employed’ was not defined in the *ITAA*. The reasonableness of the benefits that had been, were being or may have been provided for members of the fund or their dependants were taken into account by the Commissioner when approving the terms and conditions of a superannuation fund. The ‘terms and conditions’ of the fund could not permit the payment of any benefit before the member reached age 60, except in the event of death, sickness or permanent incapacity for work or in other circumstances approved by the Commissioner. They would also require that the benefits to a member or the member’s dependants be paid, or in the case of a pension, commence to be paid, before the member reached age 70.⁶⁹

The Commissioner said that he would approve a s 79 public fund or one-member fund, except in special circumstances, only if the aggregate annual contributions to superannuation funds of all classes by the member did not exceed specified amounts depending on the age of the member at the time the contribution was made.⁷⁰

The Commissioner stated in an advice issued in December 1976, that where an employer contributed to a s 79 fund, the following guidelines would apply:

Generally, where an employer chooses to contribute to a fund established and approved under section 79 of the Assessment Act the same guidelines as set out for a section 23F fund would be used in judging ‘the reasonableness of the benefits that have been, are being or may be provided for employees or their dependants from the fund.

⁶⁸ *Case G10 75 ATC 33.*

⁶⁹ *ITAA ss 79(2)(f), 79(11). Case B75 70 ATC 350.*

⁷⁰ *PIB No 6, 19 effective date 1 July 1965.*

The main difference is that, whereas in relation to a section 23F fund, the Commissioner is required only to have regard to benefits from other 23F funds, section 79 requires him to have regard to benefits received from any other superannuation fund that enjoys tax concessions under section 23(jaa) (funds established by the Australian or a State Government or by a public authority), section 23(ja) (funds for self-employed persons) and section 23F.⁷¹

In 1983, the Commissioner confirmed the past practice would continue. Wherever the law permitted, the same approaches would be applied as for s 23F funds.⁷² This guideline was later broadened to ensure that an income tax deduction allowable to an employer for contributions to a s 79 Fund would not exceed that allowable to a comparable s 23F fund.⁷³

5.2.3 Challenges by the Commissioner

The investment strategy of a s 79 superannuation fund was challenged by the Commissioner in *Case U79*. The interpretation of this case potentially applied to all superannuation funds.

In *Case U79*⁷⁴, for the 1979 income year, the Commissioner disallowed the fund the 5% cost of assets deduction under section 79(12). The Commissioner took the view that the works of art, some of which were leased to the member at an annual rental, were speculative investments which disqualified the fund from falling within s 79. The Senior Member of the AAT held that although unorthodox, the art purchased constituted sound long-term investments, and had in fact appreciated in value. In any event, the works had been acquired in accordance with powers in the trust deed which had been approved by the Commissioner, and

⁷¹ Guidelines: CCH Australia Limited, 'Tax Library' [38-525].

⁷² Taxation Ruling IT 294, paragraph 48, effective date 1 July 1982.

⁷³ Taxation Ruling 2067 paragraph 41. '... eg the discretion in *ITAA* s 82AAE(b) would not be exercised where the assets of a section 79 fund were wholly lent back to the employer.'

⁷⁴ 87 ATC 465.

it was therefore not open to the Commissioner to disallow the claim.

By substituting *ITAA* s 23FB for s 79 in 1984, the Federal Government acknowledged the inequities by making the income of these superannuation funds exempt from income tax. This provided an alternate opportunity with better tax incentives for people to save for their retirement.

5.2.4 Comment

Because the Commissioner administered s 79 superannuation funds in a similar manner to ss 23F and 23(ja) funds, alterations to the latter by default affected s 79 superannuation funds. *ITAA* s 79 was repealed because of inherent inequities in the tax incentives when compared with other superannuation funds. *ITAA* s 23FB replaced s 79 in 1984 effective on 30 June 1984 attempting to remedy the inequities.⁷⁵ With this change, income of these funds became exempt from income tax and the 5 per cent cost-of-assets deduction was abolished.⁷⁶

5.3 Section 23FB Funds

In 1983, the Federal Government considered the recommendations of a number of Committees who prepared reports on the taxation system in Australia. It recognised the importance of developing different aspects of the retirement policy for all Australians, including effectiveness of the tax incentives to encourage saving through superannuation.⁷⁷

As part of the strategy relating to the retirement policy, it introduced a new taxation arrangement for retirement and kindred

⁷⁵ Inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

⁷⁶ Minister for Housing and Construction and Minister Assisting the Treasurer, the Hon Chris Hurford MP 'Income Tax Assessment Amendment Bill (No 3) 1984' (Second Reading Speech delivered at the House of Representatives, Canberra).

⁷⁷ See Chapter 6 [6.2].

payments effective for payments made on or after 1 July 1983.⁷⁸ By 1984, the enactment of *ITAA s 23FB*⁷⁹ and the Commissioner's published advice⁸⁰ attempting to bring the requirements and assessing of all superannuation funds into line indirectly acknowledged that the provisions of the *ITAA* were inefficient and had inequities. Section 23FB funds were superannuation funds for gainfully occupied persons and replaced s 79 funds. They could be funds for self-employed persons, funds for employees who were providing their own superannuation, and/or employer-sponsored funds for employees.

Section 23FB funds offered exemption from income tax for income of the funds if they complied with the requirements of s 23FB and the in-house rule. This exemption replaced the tax relief of a special deduction equal to 5% of the cost of the prescribed assets included in the fund as at the end of the income year for s 79 funds. It corrected the inequity of different tax incentives offered to different superannuation funds and the disadvantages ensuing for the beneficiaries who were members of these funds.

Section 23FB funds continued to offer the opportunity to employees who were not covered or inadequately covered for superannuation purposes to contribute to a superannuation fund with tax incentives similar to other funds and they gave self-employed persons the opportunity to contribute to a superannuation fund with the same tax incentives as section 23(ja) without the requirement for the fund to have a minimum of 20 persons as members.

⁷⁸ Part III, Division 2, Subdivision AA - Superannuation, termination of employment and kindred payments *ITAA s 27A-27J*, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

⁷⁹ *ITAA s 23FB*, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984. applicable to assessments for the year of income commencing 1 July 1984, replaced *ITAA s 79* as repealed by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

⁸⁰ Treasurer, the Hon John Winston Howard MP 'Superannuation' (Press Release, No 68, 12 July 1979).

5.3.1 Requirements for exemption from tax

Funds that qualified for concessional tax treatment under s 79 section generally qualified for exemption under the new provisions with one significant difference. Section 79 provided that benefits could not be paid before the fund member's 60th birthday whereas s 23FB reduced that age limit to 55 years of age. Benefits had to be paid, or a pension or annuity must have commenced, not later than the member's 70th birthday.⁸¹ In the case of a right to any benefits, a pension or annuity to dependants, the terms and conditions of the fund must have stipulated that benefits had to be made or a pension or annuity had to be commenced no later than the 70th birthday of the member or on the death of a member before that birthday.⁸²

This was amended by an Income Tax Ruling to bring the normal retiring age of s 23FB funds in line with s 23F and section 23(ja) funds.⁸³ The normal retiring age was altered, effective from 1 July 1985, to 65 years for male and female employee members.

Where the fund was employer-sponsored, in addition to the requirements of s 23FB, it had to satisfy the in-house assets rules in s 121C in order to qualify for exemption from income tax.⁸⁴ This requirement removed the inefficiency of employer-sponsored funds of s 79 having an advantage over employer-sponsored s 23F funds by including in s 23FB the requirement of compliance with the in-house asset rule. The requirements of s 23F and s 23FB were the same. They were assessed under the same provisions and had the same tax advantages.

⁸¹ ITAA s 23FB(2)(f)(ii).

⁸² ITAA s 23FB(2)(f)(iii).

⁸³ Taxation Ruling IT 2201, [5], [16].

⁸⁴ ITAA s 121C(1). See Chapter 3 [3.3.2].

5.4 Life Assurance Company Superannuation Funds

Life assurance companies' funds catered for people who needed the expertise of an independent and experienced manager and trustee who could provide a vehicle eligible for the exemption of income from income tax. The disclosure required by the legislation which regulated the products offered by life assurance companies provided information to potential members about the superannuation product that they might contribute to. The added benefits provided by the life assurance companies were the mechanism for protection of members' benefits and making the trustees accountable for their responsibilities.

A life assurance company could offer superannuation products to the public. They could establish superannuation funds linked to a trust deed or the provisions of the *ITAA* or the use of a life assurance policy. Provided a superannuation fund complied with the provisions of *ITAA* and the specific requirements for that type of fund, its income could be eligible for exemption from income tax.

A 'life assurance company' was initially defined in *ITAA* as 'a company the sole or principal business of which is life assurance'.⁸⁵

In 1961, the *ITAA* was amended to define a 'life assurance company' by referencing its regulation as being under the *Life Insurance Act 1945-1959*.⁸⁶ The amendments to the *ITAA* included definitions of 'exempt superannuation fund' and 'exempt superannuation schemes' as part of a life assurance company's business for taxation purposes. At the same time, the legislation was amended to allow life assurance companies to integrate their

⁸⁵ *ITAA* s 110.

⁸⁶ Inserted by *Income Tax and Social Securities Contribution Assessment Act 1961*, No 17 1961. *ITAA* s 110 (definition of a life assurance company means 'a company 'the sole or principal business of which is life assurance and includes a company that is registered under the Life Insurance Act 1945-1959 and is carrying on life assurance business').

superannuation and overseas businesses. The legislation did not require the establishment of separate statutory funds for this business.⁸⁷ Also included in the legislation were the investment requirements to qualify for exemption of income for investment held in connection with superannuation business.⁸⁸

A life assurance company was exempt from tax on the investment income from its superannuation business subject to compliance with the provisions of the *ITAA*.⁸⁹ The company's superannuation business meant its business in connection with:

- (a) exempt superannuation funds⁹⁰;
- (b) superannuation policy⁹¹;
- (c) superannuation statutory fund⁹²; (later replaced by exempt statutory fund⁹³); and

⁸⁷ *ITAA* s 112A was inserted to provide exemption from income tax of that part of the income of a life assurance company that was referable to its superannuation business.

⁸⁸ *ITAA* s 110A.

⁸⁹ *ITAA* s 112A.

⁹⁰ *ITAA* s 110(1) (definition of 'exempt superannuation fund' was:

- (a) exempt employees' funds, both employer sponsored funds and government and semi-government funds;
- (b) self-employed persons funds;
- (c) s 79 funds, prior to 30 June 1984;
- (d) s 23FB superannuation funds from 1 July 1984).

⁹¹ *ITAA* s 110(1) (definition of 'superannuation policy' was a life assurance policy -

- (a) that was vested in the trustee of an exempt superannuation fund; or
- (b) that was -
 - (i) effected for the purposes of an exempt superannuation scheme; or
 - (ii) was accepted by the person maintaining such a scheme for the purposes of the scheme;

not being a policy that had ceased to be a policy for the purposes of such a fund or scheme).

⁹² *ITAA* s 110(1) (definition of 'superannuation statutory fund', in relation to a company, as an Australian statutory fund, or any fund, maintained by that company solely in respect of a class of life insurance business that consisted of business of, or in relation to, the issuing of, or the undertaking of liability under, superannuation policies).

Omitted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984 applicable from 1 July 1983.

Australian statutory fund, in relation to a company, meant:

a statutory fund maintained by the company under the Life Insurance Act 1945-1959 other than such a fund maintained by the company solely in respect of a class of life insurance business that did not include business of, or in relation to the issuing of, or the undertaking of liability under, Australian policies.

⁹³ *ITAA* s 110(1) (definition of 'exempt statutory fund', in relation to a company, was an Australian statutory fund, or any other fund, maintained by the company solely in respect of a class of life assurance business that consist of business of, or in relation to, issuing of, or the undertaking of liability under, eligible policies).

Inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984, applicable from 1 July 1984. Omitted by *Taxation Laws Amendment Act 1985*, No 49 1985 applicable to assessments for the year of income in which 11 September 1984 occurred.

(d) exempt superannuation schemes.⁹⁴

A life assurance company registered under the *Life Insurance Act 1945* was a prescribed corporation within the *Companies Code*.⁹⁵ These companies were regulated by legislation supervised by a government appointed body⁹⁶. This legislation included the rules relating to prescribed interests⁹⁷, fund raising from the public⁹⁸ and reporting requirements⁹⁹.

The business of life assurance companies included superannuation, life assurance and investment. The provisions of the *ITAA* relating to the taxation of life assurance companies were

-
- ⁹⁴ *ITAA* s 110(1) (definition of ‘exempt superannuation scheme meant: provident, benefit, superannuation or retirement scheme
- (a) in respect of which there is an exempt superannuation fund; or
 - (b) in respect of which there is not such fund but in respect of which the Commissioner is of the opinion that, if there were a fund in respect of the scheme, it would, having regard to the terms and conditions of the scheme, be an exempt superannuation fund).
- ⁹⁵ Before 1981, Uniform Companies Act 1961.
After 1981, Companies Code 1981: *Companies Code* subject to and in accordance with the *Companies (Application of Laws) Act 1981*, *Companies and Securities (Interpretation and Miscellaneous Provisions) (Application of Laws) Act 1981*.
- ⁹⁶ Before 1981, the Corporate Affairs Commission. After 1981, the National Companies and Securities Commission.
- ⁹⁷ *Companies Code* pt IV div 6.
Companies Code s 5 (definition of ‘prescribed interest’ as
- any right to participate or any interest, whether enforceable or not and whether actual, prospective or contingent-
 - (a) in any profits, assets or realization of any financial or business undertaking or scheme whether in the Territory or elsewhere;
 - (b) in any common enterprise, whether in the Territory or elsewhere, in relation to which the holder of the right or interest is led to expect profits, rent or interest from the efforts of the promoter of the enterprise or a third party; or
 - (c) in any investment contract, whether or not the right or interest is evidenced by a formal document and whether or not the right or interest relates to a physical asset, but does not include-
 - (d) any share in, or debenture of, a corporation;
 - (e) any interest in, or arising out of, a policy of life insurance;
 - (f) an interest in a partnership agreement, unless the agreement or proposed agreement-
 - (i) relates to an undertaking, scheme, enterprise or investment contract promoted by or on behalf of a person whose ordinary business is or includes the promotion of similar undertakings, schemes, enterprises or investment contracts, whether or not that person is, or is to become, a party to the agreement or proposed agreement; or
 - (ii) is or would be an agreement, or is or would be within a class of agreements, prescribed by the regulations for the purposes of this paragraph; or
 - (g) a right or interest, or a right or interest included in a class or kind of rights or interests, declared by the regulations to be an exempt right or interest, or a class or kind of exempt rights or interests, for the purposes of Division 6 of Part IV).
- ⁹⁸ Ibid pt IV, div 1.
- ⁹⁹ Ibid pt VI, div 1-4.

complex because the different classifications of business were within the same provisions of the *ITAA*.¹⁰⁰ Changes to the provisions of the *ITAA* for the taxation of superannuation funds under the management of life assurance companies were made to reflect the changes in provisions of the *ITAA* relating to other superannuation funds and to clarify or expand definitions within the provisions.

Only those provisions for the taxation of the superannuation business of life assurance companies, except where it is appropriate to refer to other business of these companies, are discussed.

5.4.1 *Requirements for exemption from tax*

Prior to 1 January 1961, a life assurance company could offer superannuation products to employers, self-employed persons and employees with no superannuation support from employers to participate in a superannuation fund. Exemption from tax applied to the products provided the requirements of the *ITAA* that applied to the specific type of fund offered were complied with.¹⁰¹

From 1 January 1961, the income of a life assurance company qualified for exemption from tax on the investment income referable to its superannuation business, provided the company complied with the requirements of the provisions relating to superannuation provided by life assurance companies and satisfied the 30/20 rule.¹⁰² *ITAA* Division 8 set out the requirements for compliance by life assurance companies for the income of their superannuation products to be eligible for exemption from income

¹⁰⁰ *ITAA* pt III div 8 - Life Assurance Companies, ss110-116D.

¹⁰¹ *ITAA* ss 23(j)(i), 23(ja).

¹⁰² *ITAA* ss 110A, 110A(10).

The 30/20 rule was similar to the requirement for ss 23F, 79, 23FB, 23(ja) funds. See Chapter 3 [3.3.1].

tax.¹⁰³ The exempt portion of the investment income was calculated by reference to the ratio that the calculated liabilities relating to the superannuation and specified types of annuity business bore to the total calculated liabilities relating to life business.¹⁰⁴

5.4.2 *Comments*

From 1 January 1961, life assurance companies had the responsibility imposed on them by legislation¹⁰⁵ not related to the ITAA to fully explain both the commercial and taxation implications of entering into a particular transaction.¹⁰⁶ This allowed contributors and beneficiaries to assess all liabilities and risks with certainty and make decisions with accurate knowledge.¹⁰⁷ The reporting and accounting requirements further enhanced the ongoing disclosure associated with superannuation funds managed by life assurance companies.¹⁰⁸ The choices were commercial choices related to the various products offered rather than the tax implications which, in the absence of non-compliance, were comparable. Trustees were liable for penalties for untrue or non-disclosure in documents making an offer to the public.¹⁰⁹

The restriction on the entities eligible to be life assurance companies, hence trustees of superannuation funds under the management of life assurance companies, removed the perception of potential conflict of interest.¹¹⁰ An independent trustee with

¹⁰³ *Income Tax Assessment Act 1936*, No 27 1936, amended by *Income Tax Assessment Act 1942*, No 22 1942, *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961, *Income Tax and Social Services Contribution Assessment Act (No 3) of 1964*, No 110 1964, *Income Tax Assessment Act 1973*, No 51 1973, *Statute Law Revision Act 1973-1974*, No 216 1973, *Income Tax Assessment Act 1975*, No 80 of 1975, *Income Tax Laws Amendment Act 1981*, No 108 1981 and *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

¹⁰⁴ ITAA s 112A.

¹⁰⁵ See above n 95.

¹⁰⁶ See above n 96.

¹⁰⁷ See above n 97.

¹⁰⁸ See above n 98.

¹⁰⁹ *Companies Code* s 101.

¹¹⁰ *Companies Code* s 167.

legislation regulating his duties and responsibilities made trustees accountable and protected members' benefits.¹¹¹ The requirement for auditing of financial statements provided further security for members.¹¹²

For superannuation funds offered by life assurance companies, disclosure of information to potential subscribers and on-going investors, the independent trustee and the appointment of auditors combined to protect members' benefits. This protection and tax incentives encouraged people to save for their retirement. The imposition of penalties on the trustees provided a disincentive for abuse of the legislation, both regulatory and taxation.

This use of a separate authority for the regulation of superannuation funds was considered by the Committees appointed by the Federal Government to review the structure of superannuation funds. The strategy and protective measures used by life assurance companies were recommended and later adopted by the Federal Government.¹¹³ It is unfortunate that the Federal Government took so long to respond to adopt this effective and proven structure.

5.5 Non-resident Superannuation Funds

Two types of superannuation funds provided tax benefits for those that fell into the categories of overseas superannuation funds. The first class of superannuation fund was foreign superannuation fund. Income of a foreign superannuation fund was exempt from tax provided it complied with the definition of that type of fund and the requirements of the *ITAA*. The legislation for the exempt status of these superannuation funds was introduced as a means of

¹¹¹ *Companies Code* s 174.

¹¹² *Companies Code* pt VI div 3.

¹¹³ See Chapter 6 [6.4].

encouraging overseas superannuation fund managers and trustees to invest in Australia.

The second class of overseas superannuation fund was a non-resident superannuation fund. Its income could be eligible for exemption from tax provided it complied with the requirements that applied to resident superannuation funds.

Before 1 January 1968, there was nothing in the *ITAA* to prohibit an overseas employer from establishing a superannuation fund for the benefit of employees and for the superannuation fund to be eligible for exemption for its income from income tax provided the fund complied with the requirements for exemption.

In 1968, the Federal Government, when introducing the legislation to impose withholding tax on non-residents, introduced exemption of 'foreign superannuation funds' from all income tax in respect of all income received, including interest and dividends from Australian resident companies.¹¹⁴ These amendments to the *ITAA* were as a result of the Federal Government's decision to offer overseas residents and foreign superannuation funds an incentive to invest in Australia.

From 1 January 1968, a foreign fund with no connections with Australia other than that part or all of its funds were invested in Australia was exempted from income tax for all interest and of dividends from Australian resident companies.¹¹⁵ Provided it was exempt from income tax in its own country, it was also exempt from withholding tax on such income.¹¹⁶ The trustee of a foreign superannuation fund had to obtain approval for the application of

¹¹⁴ The Treasurer, the Rt Hon William McMahon MP, 'Income Tax Assessment Bill (No 4) 1967' (Second Reading Speech delivered at the House of Representatives, Canberra).

¹¹⁵ *ITAA* s 23(jb), as inserted by *Income Tax Assessment Act (No 4) 1967*, No 85 1967 and applicable from 1 January 1968.

¹¹⁶ *ITAA* s 128B(3)(a). *ITAA* s 128B was substituted by *Income Tax Assessment Act (No 4) 1967*, No 85 1967.

this qualification.¹¹⁷ Income derived from sources wholly out of Australia by a foreign superannuation fund was exempt from tax without qualification.¹¹⁸

Overseas superannuation funds that did not comply with the requirements for foreign superannuation fund status but did comply with the same requirements for exemption status as a resident superannuation fund were treated on the same basis as a resident fund. An overseas employer could establish a superannuation fund in Australia to provide superannuation benefits for its employees in Australia, or employees of its branch or subsidiary in Australia, and allow these employees to become members of the fund. The income of such a fund, provided it complied with the exemption provisions in the *ITAA* relating to superannuation funds, could be exempt from tax.

5.5.1 Requirements for exemption from tax

Before 1 January 1968, a foreign superannuation fund could qualify for exemption from ordinary income tax under *ITAA* ss 23(ja) or 23(j)(i) or the later *ITAA* s 23F.

From 1 January 1968, *ITAA* s 23(jb) provided that income, consisting of interest or dividends paid by an Australian company, received by a foreign superannuation fund, was exempt from tax. A superannuation fund was a foreign superannuation fund if it was a provident, benefit, superannuation or retirement fund:

- (i) established outside Australia;
- (ii) had its central management and control carried on outside Australia by persons none of whom was a resident of Australia; and

¹¹⁷ Upon production of some evidence of exemption from tax in the fund's home country, eg a certificate of exemption from the relevant tax authority, a new certificate was issued exempting the fund from liability to withholding tax under Div 11A. *ITAA* s 221YM, amended by *Income Tax Assessment Act (No 4) 1967*, No 85 1967.

¹¹⁸ *ITAA* s 23(r).

- (iii) established, maintained and applied solely to provide the relevant benefits to individuals who were not or would not ordinarily have been residents of Australia or of Australia's external territories.

A fund would not qualify as a foreign superannuation fund if any contributions to it had been or were deductible or available for rebate.¹¹⁹

An overseas fund might not have come within the definition of a 'foreign superannuation fund' in the *ITAA* because:

- the fund may have included members who were residents of Australia;
- the fund may have been controlled by persons, of whom at least one was a resident of Australia or a Territory of Australia; or
- a deduction or rebate may have been allowed or allowable in Australia in respect of a contribution to the fund.

If an overseas superannuation fund did not comply with the requirement of *ITAA* s 23(jb), it may have complied with the requirements of *ITAA* ss 23(jaa) or 23F and be eligible for the exemption of its income from income tax.

5.5.2 Comments

The restricted group to which the provisions of the *ITAA* for the taxation of foreign superannuation funds applied made the requirements less complex. The members of foreign superannuation funds were not the responsibility of the Federal Government. There were no deductions for contributions nor tax concessions for payments to members. The exemption provided to these superannuation funds was to encourage investment into Australia, not encourage savings for retirement.

¹¹⁹ *ITAA* s 6(1). Definition of foreign superannuation fund was introduced by *Income Tax Assessment Act (No 4) 1967*, No 85 1967, effective from and including 1 January 1968.

5.6 Approved Deposit Funds

Approved Deposit Funds ('ADF') were introduced as a means by which an employee could change employment without having to pay tax on their eligible termination payment and preserve the entitlement for retirement. The prescribed structure of these funds provided protection of the members' benefits and made the trustees accountable for their responsibilities.

The introduction of ADFs was part of the strategy relating to the retirement policy of the Federal Government implemented in response to recommendations of a number of Committees.¹²⁰ This strategy introduced a new taxation arrangement for retirement and kindred payments effective for payments made on or after 1 July 1983. The tax on lump sum payments on the termination of employment resulted in the issue of portability being of particular importance. To coincide with the introduction of the legislation to impose tax on payments on retirement¹²¹, the Federal Government introduced into the *ITAA* a new type of fund, the ADF¹²². ADFs were investment vehicles designed to protect eligible termination payment¹²³ ('ETP') in the care of the ADFs' trustees for a limited period. Using ADFs, retirees could plan the taxation of their retirement savings effectively. Employees who changed jobs might, without paying any tax, deposit any lump sum received on termination into an ADF. The recipient of an ETP could deposit in the ADF an amount equal to all or part of that payment so the tax

¹²⁰ The Campbell Report 250 [15.99]; Task Force 9 [2.10]; 25-27 section 3 pt VII [3.58]-[3.67].

¹²¹ Part III, Division 2, Subdivision AA - Superannuation, termination of employment and kindred payments *ITAA* s 27A-27J.
ITAA ss 27A-27J, 23FA, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

¹²² The new arrangements were announced by the Treasurer in his Economic Statement of 19 May 1983 and further statements dated 30 May 1983 and 7 August 1983.

¹²³ *ITAA* s 27A(1) (definition of 'eligible termination payments' include retirement, termination and similar payments in consequence of the termination of a taxpayer's employment (including office). Superannuation fund payments were included, except those in the form of a pension or annuity).

would not be payable on that amount at the time of the roll-over.¹²⁴ A person who paid an amount into an ADF was known as a depositor. The depositor had to deposit into an ADF that part of the ETP elected to be rolled over normally within 90 days (the roll-over period¹²⁵) after receipt of the ETP. It was a legitimate way to defer tax payable on an ETP.¹²⁶ The definition of 'ETP' included the withdrawal of any amount from the ADF¹²⁷ and attracted tax¹²⁸. The depositor had to withdraw the amount rolled-over by the 65th birthday or where the depositor died, 90 days after the grant of probate or administration of the estate.¹²⁹

The trustee of an ADF invested moneys deposited to generate income. As with other superannuation funds, provided the ADF complied with the requirements in the *ITAA* s 23FA, the income was exempt from tax.¹³⁰

The Federal Government acknowledged the need for independent trustees for ADFs by requiring that the trustees be approved trustees.¹³¹ The Australian Companies and Securities Legislation regulated the invitations to the public to invest funds in ADFs and their on going reporting and management of the funds.¹³² Legislation regulating the various groups that were approved trustees specified their duties and liabilities.¹³³

¹²⁴ *ITAA* s 27B(1), C(1).

¹²⁵ *ITAA* s 27A(1) (definition of 'roll-over period' in relation to an eligible termination payment, was 'the period of 90 days commencing on the day on which the eligible termination payment is made, or such longer period as the Commissioner, in special circumstances, allows'.

¹²⁶ To obtain a roll-over exemption, the taxpayer had to complete an election in the prescribed form - *ITAA* s 27D(1)(b), Income Tax Regulation 33A.

¹²⁷ *ITAA* s 27A(1)(c).

¹²⁸ *ITAA* ss 27B, C.

¹²⁹ *ITAA* ss 27A(1) (c)(i), (ii) (definition of 'approved rules').

¹³⁰ *ITAA* s 23FA(5).

¹³¹ See above n 129.

¹³² *Companies Code 1981* pt IV, div 6 Prescribed Interests.
Corporations Act 1989 pt 7.12 div 5, Prescribed Interests.

¹³³ *ITAA* s 27A(1) (definition of 'approved trustee' included:

5.6.1 Requirements for exemption from tax

ITAA s 23FA listed the requirements for an ADF¹³⁴ to be eligible for exemption from income tax. They included that the fund must at all times during its existence in a year of income:

- be established as an indefinitely continuing fund;¹³⁵
- be maintained by an approved trustee¹³⁶ and for approved purposes¹³⁷; and
- operate under approved rules¹³⁸.

-
- (a) a life assurance company;
 - (b) an eligible bank;
 - (c) an eligible financial corporation;
 - (d) a registered corporation;
 - (e) a corporation authorised by or under a law of a State or Territory to act as executor, administrator and trustee; or
 - (f) a body that is, or is included in a class of bodies that is, prescribed for the purposes of this paragraph).

¹³⁴ ITAA s 27A(1) (definition of ADF was a fund:

- (a) that was established as an indefinitely continuing fund;
- (b) that was established solely for approved purposes; and
- (c) the rules of which, immediately after the establishment of the fund, were approved rules).

There was no reference in this definition to approved trustee or section 23FA in Subdivision AA.

¹³⁵ ITAA s 27FA(1)(a).

¹³⁶ ITAA s 27A(1). The definition of an 'approved trustee' was:

- a life assurance company registered under the *Life Insurance Act 1945*, or a public authority carrying on life insurance business through a State Government Insurance Office;
- an eligible bank, being a savings or trading bank, as defined by the *Banking Act 1959* or public authority under a State or Territory law which carries on a banking business (State Banks);
- an eligible financial corporation, being a financial corporation with the Constitution which was required to register under the *Financial Corporations Act 1974*, and including building societies, credit unions, finance companies and merchant banks whose total assets exceed \$1 million;
- a registered organisation, being a trade union, a friendly society or an association of employees registered under the *Conciliation and Arbitration Act 1904*.

¹³⁷ ITAA s 27A(1). Approved purposes for an ADF were:

- receiving on deposit amounts eligible termination payments which were rolled over within the roll-over period;
- dealing profitably with those deposits in accordance with the fund rules; and
- repaying the deposits, with accrued interest, on request by the depositor, or the legal personal representative.

¹³⁸ ITAA s 27A(1). Approved rules for an ADF:

- required the trustee to maintain records of depositors and accounts of the fund;
- required repayment to the depositor or legal personal representative of the whole of the amount deposited, with accrued income, not later than the 65th birthday of the depositor or 90 days after the grant of probate or letters of administration in relation to the estate of the depositor;
- prohibited the trustee from borrowing from, or from lending to or investing in, a related entity, except where that entity was an eligible bank;

For an approved deposit fund, private company and non-arm's length income were assessable only where that income was derived after 12 January 1987.¹³⁹

Where an ADF failed to meet the requirements for exemption, the Commissioner had a discretion to allow an exemption where he considered that there were special circumstances.¹⁴⁰ If an approved trustee did not maintain the fund as an approved deposit fund at any time during the year of income when the fund was in existence, there was no such discretion and the fund was not exempt under any circumstances.¹⁴¹ It effectively ceased to be subject to the provisions of Division 9B dealing with the taxation of superannuation funds and was taxed as an ordinary trust under the trust provisions of Division 6 of *ITAA*.

If an approved trustee maintained the fund but the fund failed to meet the requirements for exemption, unless the Commissioner disregarded the failure, its income was taxed as an ineligible ADF under the provisions of Division 9B.¹⁴² The taxable amount of an ineligible ADF was the net amount after deducting allowable deductions, other than concessional deductions¹⁴³, from its assessable income. This amount was deemed to be the taxable income of the fund.¹⁴⁴

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- prohibited the trustee from paying pensions or annuities to depositors;
 - ensured that amounts were paid to a depositor or the legal personal representative only, and then only as repayment of the whole or a part of the amount deposited, with accumulated earnings – the depositor cannot assign, transfer, mortgage or encumber his interest in the amount deposited, or the accumulated earnings;
 - required a certificate to be given each year by a registered auditor to the effect that the rules were approved and had been complied with.

¹³⁹ *ITAA* s 23FD(2), (3), (4). See Chapter 3 [3.4.3].

¹⁴⁰ *ITAA* s 23FA(2).

¹⁴¹ *ITAA* s 23FA(3).

¹⁴² *ITAA* div 9B, s 121DAA; *Income Tax (Companies, Corporate Unit Trusts and Superannuation Funds) Act*. Section 121DAA, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984, first applied for the year commencing 1 July 1983.

¹⁴³ *ITAA* s 121DD.

¹⁴⁴ *ITAA* s 121DC.

If the trustee of an ADF were to make deposited funds available for the use, either directly or indirectly, of the depositor, the fund would not have complied with the provisions. The fund would be subject to income tax and any payments made to the fund would be ineffective as roll-over payments.¹⁴⁵

5.6.2 Comments

The *ITAA* did not impose any prudential requirements on ADFs, other than those generally implicit in the definitions of ‘approved purposes’ and ‘approved rules’. Depending on the legal form of a fund, there were various prudential, disclosure and other requirements imposed on it by the general law, eg the Australian Companies and Securities Legislation¹⁴⁶.

As a result of the clarity in the provisions in the *ITAA* relating to ADFs, there were no challenges by the Commissioner relating to the income of any ADF being exempt from tax. The restriction on the entities able to hold the position of trustee removed any potential conflict of interests that were in other funds that lacked this restriction. The restrictions imposed by the definitions of the ‘approved rules’ and ‘approved purposes’ prevented abuse of ADFs. The provisions of the *ITAA* for the taxation of ADFs were less complex than other superannuation legislation because the definition of ‘ETP’ restricted the group of individuals catered for.

The introduction of ADFs by the Federal Government was the acknowledgement of the recommendations by the Committees appointed to review the structure of superannuation funds

- to encourage savings;
- amend legislation to protect members' benefits;
- make trustees accountable for their responsibilities;

¹⁴⁵ Taxation Ruling IT 2168, [51]-[53].

¹⁴⁶ *The Companies (Application of Laws) Act 1981; the Companies and Securities (Interpretation and Miscellaneous Provisions) (Application of Laws) Act 1981.*

- prevent abuse.

ITAA s 23FA was repealed as from 1 July 1986.¹⁴⁷ This coincided with the introduction of OSSA.¹⁴⁸ For the years 1986/87 and 1987/1988, income of ADFs was exempt under s 23FD provided funds met the requirements of that section.¹⁴⁹

5.7 Conclusion

To encourage people to save for their retirement, the Federal Government developed a number of types of superannuation fund to try to accommodate the various needs of those investing for their retirement. The basic principle was to provide incentives in the form of tax concessions. With a trust forming the basic structure, consideration was how to implement the mechanism to provide the tax incentives and on what criteria to base eligibility for them.

The introduction of exemption of superannuation funds established for the self-employed was the first step in expanding the opportunity for the self-employed to save with a form of tax incentive. The s 79 superannuation funds were a fall back position for those who could not or did not wish to comply with the requirements for exemption of their income from income tax. The superannuation products provided by assurance companies were another form of saving for retirement. In this instance, there were protections built into the product because of the legislation regulating them. The requirements which were later deemed to be

¹⁴⁷ Repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

¹⁴⁸ *Occupational Superannuation Standards Act 1987* received Royal Assent on 5 November 1987. It was proclaimed in accordance with *Taxation Laws Amendment Act (No 4) 1987* to commence on 21 December 1987. Transitional provisions deemed to apply from 1 July 1986.

¹⁴⁹ ITAA s 23FD was substituted for ITAA s 23FA by *Taxation Laws Amendment Act (No 4) 1987*, No 38 1987 first applicable to assessments for the year of income commencing 1 July 1986. New provisions to assess certain non-arm's length income were to be inserted in new s 121DAAA. 121DAAA, as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987, first applicable to assessment for the year of income commencing 1 July 1986.

essential for the protection of members' benefits were in the assurance companies' superannuation products. The trustee had to be an approved trustee, disclosure about the product was mandatory, the financial records had to be audited and penalties were in the legislation for non-compliance with the prudential requirements.

Similar protections were recommended by the committees in their reports to the Federal Government for the regulation of superannuation funds. Some of the regulations were included when ADFs were introduced. They required an 'approved trustee' and were to be for 'approved purposes'. The definition of 'approved trustee' required auditing of financial records.

The introduction of the definition of 'foreign superannuation fund' provided a mechanism for investment in Australia by overseas funds with the attraction of exemption of income.

The development of these superannuation funds supported the Federal Government's policy for people to save for their retirement. It did however provide a difficult position for their regulation and the interpretation of the provisions to access the tax concessions. This imprecise language also provided the opportunity for abuse of the superannuation system by the accessing of tax concessions which were not in the spirit of the legislation. Members' benefits were at risk. The Federal Government recognized this and appointed a number of committees to examine and review the superannuation system, identify anomalies, inconsistencies and unnecessary complexities in the legislation and formulate proposals to remedy any defects.

CHAPTER 6

OCCUPATIONAL SUPERANNUATION STANDARDS ACT 1987

Chapter 2 set out the background to superannuation regulation and defined critical terms. Chapter 3 detailed the exempt and concessional tax treatment of superannuation funds, this being the incentive provided by the Federal Government to encourage people to save for their retirement. Chapter 4 focused on the regulation governing superannuation funds for employees of both the private and public sectors during the period 1936 to 1986. It showed that superannuation funds for employees had been central to government policy for providing for retirement income. Chapter 5 addressed the other superannuation funds that were developed to cater for non-employees and for those employees whose employers did not provide superannuation benefits. It also addressed funds developed to allow those funds which did not comply with the requirements for exemption of their income from tax to obtain concessional tax treatment if they complied with less onerous provisions. It included discussion about the introduction of Approved Deposit Funds ('ADF') in 1984 as part of the strategy relating to the retirement policy of the Federal Government that was implemented in response to recommendations of a number of Committees. This strategy introduced a new taxation arrangement for retirement and kindred payments effective for payments made on or after 1 July 1983.

This Chapter is restricted to the analysis of the regulation of superannuation funds. It sets out the inadequacies identified by the courts and Boards of Review (in the analysis in Chapters 3 and 4) in the regulation of superannuation funds that made members' benefits vulnerable to inappropriate investment and misuse by the trustees of funds.

This Chapter reviews the various reports from Committees appointed by the Federal Government identifying anomalies, inconsistencies and complexities of the law of income tax and recommending remedies. It will demonstrate that, for superannuation legislation and regulation, the Federal Government relied on these reports for developing strategies to implement its policies. The recommendations adopted by the Federal Government heralded the commencement of a new era in the regulatory process for superannuation funds. The new legislation for the regulation of superannuation funds was the *Occupation Superannuation Standards Act 1987* ('OSSA') and its Regulations, the *Occupational Supervision Standards Regulations* ('OSSR').

This Chapter analyses the sections of OSSA and the regulations of the OSSR that incorporated measures to protect the members' benefits and ensure that the benefits would be available when required.

It will demonstrate that the legislation was developed to rectify the identified inadequacies and analyses whether it achieved and was consistent with the Federal Government's policy intent to encourage people to save for their own retirement, protect members' benefits, make trustees accountable for their responsibilities and prevent abuse.

6.1 Background

Demographic and projected economic analysis since the beginning of the 20th century confirmed the need for affirmative action in providing funding for retirement.¹ To encourage people to save for their retirement, the Federal Government developed through legislation a range of superannuation funds to provide the

¹ See Chapter 1 [1.2].

opportunity for different sectors of the community to access tax concessions.

The main types of superannuation funds developed by the Federal Government to encourage people to save for their retirement during the period 1936 to 1986 regulated by the *ITAA* were:

1. seeking exemption from income tax:
 - (i) funds established by employers for employees – s 23F² which replaced the original provisions in the *ITAA*;
 - (ii) statutory and semi-government funds – s 23(jaa)³;
 - (iii) self-employed funds – s 23(ja)⁴;
 - (iv) life assurance company superannuation funds – s 110⁵;
 - (v) foreign superannuation funds – s 23(jb)⁶;
 - (vi) approved deposit funds – s 23FA⁷; and

² *ITAA* s 23F, as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, as repealed by *Income Tax Assessment Bill 1965*, No 103 1965 inserting new provisions for s 23F, Date of Assent, commencement was 14 December 1965. Later amended by *Income Tax Assessment Act 1973*, No 51 1973, *Income Tax Amendment Act 1981*, No 108 1981, *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

³ *ITAA* s 23(jaa), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964. Later amended by *Statute Law Revision Act 1973-1974*, No 216 1973, as repealed by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989.

⁴ *ITAA* s 23(ja), as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1952*, No 90 1952. Later amended by *Income Tax Assessment Act 1965* No 103 1965, *Income Tax Laws Amendment Act 1981*, No 108 1981, as repealed by *Taxation Laws Amendment Act (No 4) 1987* No 138 1987.

⁵ *ITAA* div 8, ss 110 - 116D, as amended by *Income Tax Assessment Act 1942*, No 22 1942, *Income Tax and Social Services Contribution Assessment Act 1961*, No 17 1961, *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, *Income Tax Assessment Act 1973*, No 51 1973, *Statute Law Revision Act 1973-1974*, No 216 1973, *Income Tax Assessment Act (No 2) 1974*, No 126 1974, *Income Tax Assessment Act 1975*, No 80 1975, *Income Tax Laws Amendment Act 1981*, No 108 1981.

⁶ *ITAA* ss 23(jb), 6(1) (definition of a 'foreign superannuation fund'), as inserted by *Income Tax Assessment Act (No 4) 1967*, No 85 1967, effective from 1 January 1968.

⁷ *ITAA* s 23FA, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984 applicable to assessments for the year of income commencing 1 July 1983, repealed by *Taxation Laws Amendment Act No 4) 1987*, No 138 1987. *ITAA* s 23FD, as inserted by *Taxation Laws Amendment Act No 4) 1987*, No 138 1987 first applicable to assessments for the year of income commencing 1 July 1986 to coincide with the introduction of the *Occupational Superannuation Standards Act*.

Part of superannuation benefits, inter alia payments on termination, became liable to tax effective from 1/7/83. *ITAA* ss 27A-27J, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984. See Chapter 5 [5.6].

2. seeking tax relief when non-compliant - superannuation funds for employees and self-employed funds - s 79⁸. Section 23FB replaced s 79 in 1984.⁹

Each type of superannuation fund had specific requirements that had to be complied with to have the exemption or concessional tax treatment applied to it.

During the 1970s and the early 1980s, Australia experienced an increase in the application of tax avoidance¹⁰ techniques, including accessing the exemption and concessional treatment of income from income tax by using the provisions relating to superannuation funds. The Commissioner challenged the application by taxpayers of provisions of the *ITAA* relating to concessional tax treatment of transactions involving superannuation funds, especially in circumstances not intended by the Federal Government's policy to encourage savings for retirement. The challenges by the Commissioner exposed a number of inadequacies. These included inappropriate investment by trustees of superannuation funds and dissipation of members' entitlements.¹¹

⁸ *ITAA* s 79, as repealed by and inserted by *Income Tax and Social Services Act (No 3) 1964*, No 110 1964. Later repealed by and new provisions for *ITAA* s 79 inserted by *Income Tax Assessment Act 1965*, No 103 1965, later amended by *Income Tax Assessment Act 1973*, No 51 1973, *Income Tax Laws Amendment Act 1981*, No 108 1981, as repealed by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

⁹ *ITTA* a 23FB, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984 applicable to assessments for the year of income commencing 1 July 1984. The introduction of *ITAA* s 23FB was part of the strategy for the new retirement policy to encourage savings for retirement and protect members' benefits and remove inequities in the provisions relating to the regulation of superannuation funds. *ITAA* s 23FB removed the inefficiency of *ITAA* s 79 employer-sponsored funds having an advantage over s 23F employer-sponsored funds by including in *ITAA* s 23FB the requirement of having to comply with the 'in-house asset rule'. The requirements of *ITAA* ss 23F and 23FB were the same. They were assessed under the same provisions and had the same tax advantages.

¹⁰ Chapter 1 [1.4] n 78.

¹¹ See Chapter 4 [4.3.3].

The issues identified as inadequate for the protection of the Revenue and members' benefits in the superannuation funds established by employers for employees in *ITAA* s 23F included:

- the employer, or a related party, lending funds, often interest free, to the superannuation fund that then earned income that was exempt from income tax¹²;
- the employer, or a related party, making contributions to the superannuation fund to obtain a tax deduction for the contributions and the superannuation fund then participating in one or all of the following:
 - (i) lending the contributions back to the employer, or a related party, often interest free;¹³
 - (ii) purchasing shares in the contributing employer, or a related party, providing capital back to the company and subsequently a means of distributing profits to the superannuation fund that were exempt from income tax;¹⁴
 - (iii) not advising employees of the existence of their rights to benefits nor defining the rights of individual employees so that any claim for the rights would be unlikely;¹⁵
 - (iv) terminating employees before they became eligible for any entitlement of benefits so that when the trustee wound up the fund the only employees remaining to

¹² *Associated Provident Funds Pty Limited v FC of T* (1966) 14 ATD 333; *Case C49 71* ATC 225; *Case U174 87* ATC 998.

¹³ *Case L13 79* ATC 72; *FC of T v Roche* 91 ATC 5024. Taxation Ruling IT 2067 [31] announced that this practice could result in the exemption previously granted to the fund and deductions for contributions allowed to the employer being re-examined. It may be concluded that the fund had not at all times since its inception been maintained solely for the purposes of providing superannuation benefits.

¹⁴ *Associated Provident Funds Pty Limited v FC of T* (1966) 14 ATD 333; *Compton v Commissioner of Taxation of the Commonwealth of Australia* (1965) 39 ALJR 400; *Case B15 70* ATC 61; *Driclad Pty Ltd v Commissioner of Taxation of the Commonwealth of Australia* (1966) 121 CLR 45.

¹⁵ *Case U227 87* ATC 1265; *Case W109 89* ATC 859; *Case X16 90* ATC 180; *FC of T v Roche* 91 ATC 5024.

receive benefits of the fund were parties related to the employer;¹⁶

- the superannuation fund borrowing money and purchasing shares with this money in the contributing employer or a related party, providing capital to the company and a means of distributing profits which were exempt from income tax;¹⁷
- the employer, or a related party, making excess contributions to the superannuation fund to obtain a greater tax deduction and/or accumulating amounts in the superannuation fund in excess of the provisions required to provide benefits for employees;¹⁸
- the employer, or related party, making ‘catch-up’ contributions for persons close to retirement¹⁹.

These inadequacies undermined the Revenue and members’ benefits by allowing abuse of the legislation and the Federal Government’s policy to encourage people to save for their retirement. They indicated that there were motives other than providing members’ retirement benefits for establishing superannuation funds. The inadequacies in *ITAA s 23F* that related specifically to members’ benefits:

- allowed the trustee of a superannuation fund:
 - to make loans to employers or related parties;
 - to invest in the employer or related parties; and
 - not to inform employees of their entitlement to benefits within the superannuation fund;
 - allowed an employer to terminate an employee before that employee became eligible for any entitlement of benefits.
- Employees not having legal rights to their superannuation

¹⁶ *Raymor Contractors v FC of T* 90 ATC 4684; *Bayton Cleaning Company Pty Limited v FC of T* 91 ATC 4076.

¹⁷ *Compton v Commissioner of Taxation of the Commonwealth of Australia* (1965) 39 ALJR 400.

¹⁸ *Case A69 69* ATC 385.

¹⁹ *Case W82 89* ATC 722.

benefits precluded their being able to challenge the employer or the trustee of the superannuation fund to secure the benefits.²⁰

The main defect in the legislation for superannuation funds established for self-employed persons under *ITAA* s 23(ja) was the onerous requirement to have more than twenty participants in the superannuation fund. Whilst the number of participants was a form of protection for the members' benefits, it was a deterrent for self-employed persons to save for their retirement. The alternatives for self-employed persons included:

- establishing a superannuation fund to comply with the requirements of *ITAA* s 79;
- investing in a superannuation policy with a Life Assurance Company; or
- incorporating their business so that making contributions to a superannuation fund was an option available to save for retirement assisted by tax concessions. This option was not available to some professional persons because of the restrictions imposed by their professional associations.²¹

The requirements of the *ITAA* (and the inadequacies) for s 79 superannuation funds which were funds established for gainfully employed persons were substantially the same as for superannuation funds established by employers for the benefit of employees under *ITAA* s 23F but with less taxation benefits.²²

There were no accounting, auditing or reporting provisions for superannuation funds within the provisions of the *ITAA*. From 1

²⁰ See Chapter 4 [4.3.5].

²¹ See chapter 5 [5.1].

²² Income of superannuation funds that complied with *ITAA* s 79 was eligible for concessional taxation treatment as opposed to exemption from income tax.

July 1982, an independent auditor²³ was required, every year in the case of a loan back fund, and every three years in the case of other funds, to provide a certificate verifying that the assets of the fund:

- actually existed in the fund;
- were in a form suitable for the purpose for which they existed, ie that in the event of retirement or resignation of employees, the assets were readily realisable; and
- indicating whether, in the opinion of the auditor, the fund was being conducted in accordance with its constituent document.²⁴

Whilst these inadequacies identified in *ITAA* ss 23F, 23(ja) and 79 by the Commissioner and the courts and Board of Review were potentially present in superannuation funds established by Life Assurance Companies, the presence of an independent party to operate these funds was effectively a protection for the entitlement of members.²⁵ A life assurance company registered under the *Life Insurance Act 1945* was a ‘prescribed corporation’ within the Companies Code.²⁶ These companies were regulated by legislation supervised by a government appointed body²⁷. This legislation

²³ Taxation Ruling IT 2067 [37].
The auditor need not be a registered company auditor. Membership of either the Institute of Chartered Accountants in Australia or the Australian Society of Accountants was sufficient qualification for the purpose of auditing a fund and supplying a compliance certificate.

²⁴ Taxation Ruling IT 294 [46-47].

²⁵ *ITAA* s 110 (definition of exempt superannuation fund refers to a fund established or maintained in accordance with ss 23(jaa), 23F, 23(ja)).

²⁶ Before 1981, Uniform Companies Act 1961.
After 1981, *Companies Code 1981: Companies Code* subject to and in accordance with the *Companies (Application of Laws) Act 1981* and the *Companies and Securities (Interpretation and Miscellaneous Provisions) (Application of Laws) Act 1981*.

²⁷ Before 1981, the Corporate Affairs Commission. After 1981, the National Companies and Securities Commission.

included the rules relating to prescribed interests²⁸, fund raising from the public²⁹, auditing and reporting requirements³⁰.

To address the inadequacies in legislation relating to the regulation of superannuation funds, the Federal Government appointed a number of Committees to examine existing legislation and the operation of the legislation and to identify any anomalies, inconsistencies and unnecessary complexities. These Committees were to formulate proposals for remedying the identified inadequacies. The maintenance of the Revenue was a prime concern but specific terms of reference applied to the instructions of the Committees. The Federal Government relied on the Reports from these Committees to formulate their policies.

6.2 Reports to the Federal Government

The Federal Government appointed a number of Committees³¹ to review the taxation legislation during the 1970s and early 1980s. Some of these Committees reviewed superannuation as part of a general review of the taxation system. Others were appointed specifically for the review of the superannuation system. After considering the reports from these Committees and advice from bodies,³² the Federal Government³³ recognised that whilst the encouragement for saving for retirement was effective,³⁴ there were anomalies that made the superannuation system inequitable and vulnerable to abuse. There was a need for stricter regulation if members' benefits and the Revenue were to be protected and to ensure that superannuation arrangements were directed at meeting genuine retirement needs.³⁵ Only those aspects of the Reports relating to the protection of members' benefits are

28 *Companies Code* pt IV div 6.

29 *Ibid* pt IV div 1.

30 *Ibid* pt VI div 1-4.

discussed here except where statements by the Committee are necessary to explain the context of their recommendations.

The Reports relevant to the regulation of superannuation funds, identified by the names by which they became known, were:

1. the Ligertwood Report;
2. the Asprey Report;
3. the Hancock Report;
4. the Campbell Report, and
5. the Task Force.³⁶

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- 31
- Commonwealth Committee on Taxation, Commonwealth Government of Australia, *Report of the Commonwealth Committee on Taxation* (1961), 'Ligertwood Report'.
 - Taxation Review Committee, Commonwealth Government of Australia, *Full Report* (1975), 'Asprey Report'.
 - Committee of Inquiry, Commonwealth Government of Australia, *A National Superannuation Scheme for Australia* (1976), 'Hancock Report Part One'.
 - Committee of Inquiry, Commonwealth Government of Australia, *Occupational Superannuation in Australia* (1977), 'Hancock Report Part Two'.
 - Committee of Enquiry, Commonwealth Government of Australia, *Australian Financial System* (1981), 'Campbell Report'.
 - Commonwealth Taskforce, *Occupational Superannuation* (Parliamentary Paper No 27, Parliamentary Library, Commonwealth Government of Australia, 1983), 'Task Force Report'.
- 32 Life Insurance Federal of Australia, the Association of Superannuation Funds of Australia and the Institute of Actuaries of Australia.
- 33 The Australian Labor Party government under the Prime Minister Rt Hon Robert James Hawke, AC.
- 34 Prior to 1970s, superannuation coverage was generally limited to higher paid white-collar staff in large corporations, employees in the finance sector, public servants and members of the Defence Force.
APRA, 'A recent history of superannuation in Australia' (2007) *APRA Insight Issue 2* (Special edition).
Proportion of people aged 15 years and over with superannuation coverage increased from 28% in February 1974 to 34% in November 1988 (only people with a superannuation account attracting contributions were defined as having superannuation coverage) to 60% in November 1991.
ABS 'Australian Social Trends' *Trends in Superannuation Coverage* 2009 4102.0 .
The Campbell Committee reported in its Interim Report [5.127] that the assets of public and private superannuation funds increased from 5% to 9% of the total assets of financial institutions over the two decades to 1970 and at the date of the Report in 1981 at about 8%.
- 35 Minister for Employment Services and Youth Affairs and Minister Assisting the Treasurer, the Hon Allan Clyde Holding M P, 'Occupational Superannuation Standards Bill 1987' (Second Reading Speech at the House of Representatives, Canberra, 18 September 1987).
- 36 See above n 31.

Each Report identified issues that the Federal Government needed to address to ensure the successful implementation of their policy intent for people to save for their own retirement. The terms of reference for the Committees varied. In some reports, superannuation was part of an overall review of the taxation³⁷ or the financial system³⁸ or included its interaction with social and economic policies. In other reports, superannuation was the central topic.³⁹ The Committees reviewed and referred to the Reports of previous Committees, in some instances agreeing with their conclusions and in others dissenting.

6.2.1 *The Ligertwood Report*

The review by the Ligertwood Committee, appointed by the Federal Government⁴⁰ in 1959 with its response in 1961, identified a number of inadequacies in *ITAA* s 23(j)(i). This section was the original general provision for the exemption of superannuation funds established by an employer for the benefit of employees. The Report addressed the abuse of the provisions in the *ITAA* by some employer taxpayers accessing exemption and tax benefits for income. It also addressed the need to secure members' benefits and make the members aware of their benefits.⁴¹ This review by the Ligertwood Committee resulted in the introduction of *ITAA* ss 23F⁴² and 23(jaa)⁴³ in 1964. The substituted sections provided a continuation of the exemption in s 23(j)(i) but defined the

³⁷ The Ligertwood Report; the Asprey Report.

³⁸ The Campbell Report.

³⁹ The Hancock Report; the Task Force Report.

⁴⁰ Liberal-Country Party coalition government under the Prime Minister the Rt Hon Robert Gordon Menzies KC (later, Sir Robert, KT, CH, QC).

⁴¹ See Chapter 4 [4.2.3].

⁴² Exemption of income of superannuation funds established for the benefit of employees, as inserted by *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, Date of Assent, commencement 23 November 1964.

⁴³ Exemption of income of superannuation funds established for the benefit of employees of government or other public authorities, as inserted by amendment *Income Tax and Social Services Contribution Assessment Act (No 3) 1964*, No 110 1964, Date of Assent, commencement 23 November 1964.

application of the provisions more clearly. The changes implemented in the new s 23F were to protect both the Revenue and members' benefits.

6.2.2 *The Asprey Report*

In 1972, the Treasurer of the Federal Government⁴⁴ announced a full-scale public inquiry into the overall operation of the taxation system by a Committee to be appointed. This Committee, the Taxation Review Committee, became known as 'the Asprey Committee'. The inquiry was to review the tax policy.⁴⁵ The Asprey Committee was directed to carry out its review 'in light of the need to ensure a flow of revenue sufficient to meet the revenue requirements of the Commonwealth.'⁴⁶ The Committee believed that the exemption from tax available to most superannuation

⁴⁴ Liberal-Country Party coalition government under Prime Minister Rt Hon William McMahon CH (later Sir William, GCMG). After the change of Government following the election on 2 December 1972, the new Federal Government, the Australian Labor Party under the Prime Minister the Rt Hon Edward Gough Whitlam, AC, QC confirmed the Asprey Committee's appointment.

⁴⁵ The Asprey Report, Preface i.

1. The functions of the Committee of Inquiry are –
 - (a) to examine and inquire into the structure and operation of the present Commonwealth taxation system;
 - (b) to formulate proposals for improving the Commonwealth taxation system, either by way of making changes in the present system, abolishing any existing form of taxation or introducing new forms of taxation; and
 - (c) to report to the Treasurer of the Commonwealth accordingly.
2. The Committee of Inquiry shall, in carrying out its functions, do so in the light of the need to ensure a flow of revenue sufficient to meet the revenue requirements of the Commonwealth and have regard to –
 - (a) the effects of the present Commonwealth taxation system, and of any proposals formulated by the Committee, upon the social, economic and business organisation of the community and upon the economic and efficient use of the resources of Australia; and
 - (b) the desirability of the Commonwealth taxation system being such that, so far as is practicable, there is a fair distribution of the burden of taxation, and revenue is raised by means that are not unduly complex and do not involve the public or the administration in undue difficulty, inconvenience or expense.
3. For the purposes of these terms of reference, the present Commonwealth taxation system shall be taken to be the system under which the Commonwealth raises revenue by means of the following forms of taxation:–
 - Income Tax
 - Sales Tax
 - Estate Duty
 - Gift Duty
 - Duties of Excise imposed for the purpose of raising general revenue, and duties of Customs that correspond with duties of Excise so imposed.

⁴⁶ Ibid [3.3].

funds was justified. It stated that it encouraged ‘the provision of the future needs of employees by themselves and by employers recognising a moral obligation’.⁴⁷ The Asprey Committee further stated that the exemption served to correct the bias against saving inherent in a system of tax on income and helped to promote capital formation.⁴⁸

The Asprey Committee considered the number and variety of superannuation schemes in existence and that the associated diversity of provisions in the *ITAA* made effecting any change difficult. To facilitate any changes to the regulation and taxation of superannuation funds, the Committee recommended the creation of a single category of approved funds. This recommendation excluded provisions relating to foreign superannuation funds.⁴⁹

Only transactions⁵⁰ involving approved superannuation funds would have concessional tax treatment.⁵¹ To be an approved fund, the Asprey Committee’s suggestion was that an employee’s interest in the employer’s contribution had to be vested in the employee/member, a factor considered essential for the approval of a superannuation fund.⁵² It was suggested that there needed to be some assurance that the savings accumulated in a superannuation fund were long-term savings⁵³ and would ‘only provide benefits in the event of age retirement or earlier death or ill health’.⁵⁴ It was further suggested that the trustee of a superannuation fund should be ‘debarred from investing (except to a minor extent) in

⁴⁷ Ibid [21.94].

⁴⁸ Ibid.

⁴⁹ Ibid [21.97].

⁵⁰ Benefits paid to employees, contributions made to the superannuation fund and exemption from tax on income of approved deposit funds.

⁵¹ The Asprey Report [21.119].

⁵² Ibid [21.111], [21.114], [21.119].

⁵³ Ibid [21.96(b)].

⁵⁴ Ibid.

shares of or loans to an employer of the members of the fund'.⁵⁵ It was stated that such 'investment' was undesirable as the security of the members' benefits was put at risk. If the employer's business failed employees would lose not only their jobs but also that part of their superannuation benefits that was represented by the investment.⁵⁶ The Asprey Committee considered that the *ITAA* should be amended so that annuities sold to the trustees of superannuation funds should be classified as superannuation policies.⁵⁷ These measures of vesting and restricting payment of benefits and investment in the employer of members, would provide a mechanism for identifying and protecting a member's entitlement.

The Asprey Committee suggested that limitations should be imposed on the amount of fund income exempted from tax.⁵⁸ Preferably this would be achieved by the imposition of limits on the benefits that could be provided by such funds to members and thus, indirectly, on the assets and income of the funds.⁵⁹ This limitation would protect the Revenue from abuse.⁶⁰

The review by the Asprey Committee resulted in two views. The first view stated that the basic structure of the superannuation and other retirement provisions in the *ITAA* should be left untouched. The second view recommended some fundamental changes.⁶¹ These views included the following relating to the regulation of superannuation funds and the protection of members' benefits:

55 Ibid [21.101].

56 Ibid.

57 Ibid [21.78]-[21.79].

58 Ibid [21.96].

59 Ibid [21.96(a)].

60 The calculation of reasonable retirement benefits associated with a common retiring age of 65 was adopted in IT 2201, 1 July 1985.

61 The Asprey Report [21.58]-[21.60].

1. the creation of a single category of approved funds excluding foreign superannuation funds;⁶²
2. only transactions involving approved superannuation funds would have access to concessional tax treatment in the *ITAA*;⁶³
3. to be an approved fund, an employee's interest in the employer's contribution had to be vested in the employee/member;⁶⁴
4. the savings accumulated in a superannuation fund would be long-term savings and would only be provided as benefits in the event of age retirement or earlier death or ill health;⁶⁵
5. the trustee of a superannuation fund should be debarred from investing (except to a minor extent) in shares of or loans to an employer of the members of the superannuation fund;⁶⁶
6. limitations should be imposed on the amount of fund income exemption.⁶⁷

6.2.3 *The Hancock Report*

In 1973, the Federal Government⁶⁸ appointed the National Superannuation Committee of Inquiry, known as the 'Hancock Committee'. The Report was presented in two parts. Part One of the Hancock Committee's Final Report, entitled *A National Superannuation Scheme for Australia*,⁶⁹ dealt with 'publicly provided benefits available to the whole community'.⁷⁰ Part Two⁷¹ was

⁶² Ibid [21.97].

⁶³ Ibid [21.119].

⁶⁴ Ibid [21.111], [21.114], [21.119].

⁶⁵ Ibid [21.96(b)].

⁶⁶ Ibid [21.101].

⁶⁷ Ibid [21.96].

⁶⁸ Labor Party under the Prime Minister the Rt Hon Edward Gough Whitlam, AC, QC.

⁶⁹ Commonwealth of Australia, *Final Report of the National Superannuation Committee of Inquiry Part One* Parl Paper No 155 (1976). See Chapter 1 [1.4] for discussion on the recommendation of a National Superannuation Scheme.

⁷⁰ Ibid vii.

concerned with ‘aspects of occupational superannuation and related forms of retirement provisions’.⁷²

The Hancock Committee perceived the role of occupational superannuation to be complementary to that of national pensions.⁷³ This perception influenced the Hancock Committee’s analysis of and recommendations relating to the occupational superannuation schemes. As a result, the Hancock Committee identified in their Report a number of problems in the superannuation arrangements. The problems relating to the protection of members’ benefits included:

- (1) the erosion of benefits payable on retirement, death or disablement by the partial forfeiture of accrued entitlements on withdrawal from service and the non-preservation of vested benefits,
- (2) ...
- (3) the disparity of employer support as between some public sector schemes and most schemes in the private sector,
- (4) ...
- (5) ...
- (6) the unfavourable treatment of self-employed persons under taxation provisions affecting superannuation, and
- (7)⁷⁴

The Hancock Committee stated that the problems identified influenced its approach to its review. Its recommendations implied the construction and operations of occupation superannuation schemes should conform to certain standards.⁷⁵ From this, it followed that to be eligible for taxation concessions, compliance by a superannuation fund with these prescribed standards was essential.

⁷¹ Commonwealth, *Final Report of the National Superannuation Committee of Inquiry Part Two* Parl Paper No 70, (1977).

⁷² Ibid vii.

⁷³ Ibid viii, 1 [1.1], 28 [3.5].

⁷⁴ Ibid viii-ix, 38 [3.35], 35 [3.26], 41 [3.46].

⁷⁵ Ibid ix.

For the construction of the superannuation schemes, the Hancock Committee agreed with the Asprey Committee that the diversity of provisions of the *ITAA* should be eliminated and a single category of approved funds created.⁷⁶ It stated that little further delay was warranted in respect of, *inter alia*, the creation of a single category of approved superannuation fund.⁷⁷ There were similar problems for public service and related superannuation schemes established by an Act of the Commonwealth or State or an Ordinance of a Territory. There was a diversity of rules and regulation with different levels of support for employees. Public service and related superannuation schemes should be reviewed and be modified where necessary by direct legislation and regulation.⁷⁸

The Hancock Committee also addressed the regulation of superannuation schemes. It recommended that the responsibility for compliance with the conditions of approval remain with the Commissioner of Taxation with increased actuarial assistance and much reliance placed upon undertakings given by trustees.⁷⁹ Legislation should be amended to confer power on trustees in relation to the operations of the superannuation funds.⁸⁰ The Committee introduced the concept of a tribunal to give aggrieved members a right to appeal.⁸¹

⁷⁶ Ibid ix, 126 [8.15]; The Asprey Committee [21.97].

⁷⁷ Ibid xv, 126 [8.15].

⁷⁸ Ibid viii-x, xv, 69-70 [5.24]-[5.26].

⁷⁹ Ibid ix, 55-6 [4.31]-[4.34].

⁸⁰ Ibid ix, 56-8 [4.35]-[4.39].

These powers would be:

1. To give such undertakings to the Commissioner of Taxation as are necessary to secure the approval of funds and to act in accordance with those undertakings,
2. To adjust benefits and contributions in ways that are reasonably related to the extended provisions of national pensions, and
3. With the consent of individual beneficiaries, to replace lump sum benefits with pensions.

It recommends that no modification of occupational schemes which would reduce accrued entitlements be permitted.

⁸¹ Ibid ix, 58-9 [4.40].

When considering the operations of superannuation schemes, the Hancock Committee recognised that the provisions of superannuation schemes may erode members' benefits in two ways:

1. the withdrawal benefit is less than the amount that might reasonably be regarded as accrued up to the time of the member's withdrawal; and
2. the withdrawal benefit is paid in cash at the time of withdrawal rather than deferred until retirement, death or disablement.⁸²

It took the view that concessional treatment for superannuation schemes should be confined to schemes that made reasonable provisions for the vesting and preservation of accrued benefits.⁸³ The Report noted that the concept of vesting, preservation and portability of benefits had been under consideration for some years.⁸⁴

The Hancock Committee identified three main issues relating to vesting:

1. the basis upon which benefits accruing during service are vested in the member;
2. the manner in which accrued benefits are to be identified; and
3. the nature of the transitional arrangements (if any) for the introduction of vesting requirements.⁸⁵

It noted that while vesting encouraged stability of staff employment for an employer, vesting should not provide a disincentive for employees to take alternative employment. The Hancock Committee was also conscious that compulsory vesting might

⁸² Ibid 82 [6.1].

⁸³ Ibid.

⁸⁴ In 1965, the Treasurer, the Rt Hon Harold Holt, requested Sir Leslie Melville to report on possible ways of protecting the rights of employees. His report was presented in February 1968 but has not been made public.
T H Kewley *Social Security in Australia 1900-72* (Sydney University Press) 426.

⁸⁵ The Hancock Report 83 [6.4].

discourage employers from providing superannuation regarding it as a 'fringe' benefit'.⁸⁶ The Report quoted the Institute of Actuaries:

An employer compelled to grant full vesting might avoid or minimise any additional costs by one or more of the following means:

- (1) Reducing the scale of retirement, death and disablement benefits.
- (2) Increasing the employee's contributions (if any).
- (3) By imposing conditions or extending the existing conditions under which employees were admitted to the scheme.

This would be a risk that some employers might wind up their existing schemes in order to set up unfunded schemes, to which vesting provisions might not apply. Other employers might be dissuaded from establishing schemes they had in mind. However, too much should not be made of these possibilities, for experience in other countries suggests that the introduction of controlling legislation has not had these results.⁸⁷

For vesting to be effective and provide for retirement, death and disablement as intended by the Federal Government by giving taxation advantages to superannuation funds, the Hancock Committee stated that vested benefits must be preserved. As there was no prohibition in the *ITAA* on cash payments of superannuation benefits on withdrawal from service, leaving an employer's service represented an opportunity to access this cash.⁸⁸

Various methods of preservations were suggested: 'cold storage' (ie retention in the superannuation fund), transfer to the superannuation fund of another employer, the transfer of title to a life insurance policy, the purchase of a deferred annuity and payment into a public superannuation fund.

⁸⁶ Ibid [6.5].

⁸⁷ *Vesting and Preservation of Employee Superannuation Benefits in Australia* 1968.

⁸⁸ *ITAA* s 23F(2)(e) provided that the right to receive benefits was defined by the terms and conditions applicable to the fund.

On the matter of costs of vesting benefits, the Hancock Committee commented that these would be borne by various parties. It referred to the 1968 statement of the Institute of Actuaries⁸⁹:

To compel preservation of already vested benefits would make little difference to employer's costs. When the preserved benefit is a transfer of value or paid-up policy benefit there is not extra cost involved over that of paying the vested benefit in cash. Cold storage benefits, however, give the employer a continuing burden of administration until they eventually come to be paid.

The statement commented on the overall cost of vesting and preservation:

There are so many separate factors involved in extending vesting and preservation that it is difficult to estimate the likely overall cost in the absence of specific proposals. An accurate estimate would in any case be impossible because of the dearth of information about superannuation schemes. So far as employers are concerned, the cost of full vesting might be quite large in absolute terms, even if it appeared small in relation to employers' total costs.

To prevent abuse of the preservation requirement, the Hancock Committee suggested that a minimum retirement age should be specified.⁹⁰

The Hancock Committee addressed the question of possible measures to ensure the availability of funds for payment of members' benefits when claimed. It noted that there was no obligation under the provisions in the *ITAA* to provide a mechanism for funding members' benefits. The Committee recommended:

[with] a view to decreasing the risk that members of funded superannuation schemes will be adversely affected by inadequate funding or investment losses, ...

1. that in benefit promise schemes, other than schemes wherein benefits are funded through life insurance policies, actuarial reviews of the employers' contribution rates be undertaken at

⁸⁹ See above n 87.

⁹⁰ The Hancock Report xi; 93 [6.36]-[6.38].

- intervals not exceeding three years and the employers be required to contribute at rates certified as appropriate by the actuaries,⁹¹
2. that no scheme involving the use of unallocated funds be approved unless the trust deed or similar document commits the employer, in the event of the scheme's being terminated, to make whatever payments are necessary to ensure that accrued benefits are honoured,⁹² and
 3. that no more than 10 per cent of the assets of a fund, measured in book values, consist of equities in or loans to the employer's business unless the investment asset is so secured that its value is not dependent upon the employer's survival. (In the case of a scheme open to employees of two or more businesses, there should be a further limit of 15 per cent on investments in the two businesses; if there are three or more employers, the limit should be 20 per cent.).⁹³

The Committee does not support the creation of an insurance scheme to guarantee the payment of benefits in the event of fund termination.⁹⁴

The Hancock Committee supported the recommendation by the Asprey Committee that the *ITAA* should be amended to allow life insurance companies to classify annuities as superannuation policies when sold to trustees of superannuation schemes.⁹⁵

The Hancock Committee stated that the actions of trustees and administrators should be open to scrutiny. To achieve this, it recommended:

1. that the trustees or managers of a scheme using unallocated funding be required to obtain an actuarial report when the scheme is set up and thereafter at least triennially,
2. that the trustees or managers be required to prepare annual reports,

⁹¹ Ibid 102-3 [7.5]-[7.7].

⁹² Ibid 103-4 [7.8]-[7.4].

⁹³ Ibid 104-5 [7.13]-[7.17].

⁹⁴ Ibid xii, 104 [7.12].

⁹⁵ Ibid xiii, 106-108 [7.22]-[7.25]; the Asprey Report [21.78].

3. that the annual report of a scheme include annual accounts, together with a report on the accounts by a professionally qualified auditor,
4. that the annual report provide information about the investments of the fund,
5. that the annual report for a scheme using unallocated funding include actuarial statements, prepared at the most recent valuation showing;
 - (i) the extent to which accrued benefits would be secured on the immediate discontinuance of the scheme, and
 - (ii) the rate of contribution recommended, the bases used in making the recommendation and the level of funding which it was intended to achieve,
6. that the annual report for an accumulation scheme include a statement of the method used in valuing members' interests in the fund, and
7. that in an accumulation scheme the accumulated benefits of each member be determined annually and communicated to the member.

For schemes wherein contributions are used to buy individual life insurance policies, the Committee recommends that the trustees be required to give each member annual statements of the sums assured and bonuses in force.⁹⁶

The Hancock Committee questioned the ability of the Federal Government to legislate with respect to superannuation in relation to those other than employees in the Commonwealth public sector. It received advice from Professor Geoffrey Sawer.⁹⁷ The following points accord with that advice:

1. Legislation to regulate funded superannuation schemes can probably be supported under section 51(xiv) (the insurance power). However, this section explicitly excepts State insurance unless it extends beyond the limits of the State concerned. Consequently, some schemes established under State legislation would probably not fall within the Commonwealth's insurance power.

⁹⁶ Ibid xii, 105-6 [7.18]-[7.21].

⁹⁷ Formerly Professor of Law in the Research School of Social Sciences at the Australian National University.

2. The Commonwealth Parliament can tax private superannuation funds and the benefits paid from them. Likewise, it can exempt funds which conform to specified standards.
3. The power to tax funds and benefits paid by them probably extends to funds established under State legislation, provided that the taxation provisions do not discriminate against such funds;
4. Taxation deductions and rebates can be granted for contributions to superannuation funds and for unfunded benefit payments. These deductions and rebates may be conditional upon compliance with stated criteria.⁹⁸

On the basis that *Constitution* s 51(xiv) (the insurance power) might have restricted some of their recommendations and suggestions to modify the operation of existing schemes, the Hancock Committee preferred reliance on the *Constitution* s 51(ii) (the taxation power) as being more certain than the scope of the insurance power.⁹⁹

In summary, for purposes of regulation of superannuation funds, the Hancock Committee recommended:

1. one category of approved superannuation fund, including both public sector funds and private sector funds;
2. compliance with the prescribed standards for favourable treatment under taxation legislation;
3. that the Commissioner of Taxation be responsible for compliance with the conditions of approval, with increased actuarial assistance and much reliance placed upon undertakings given by trustees.
4. life insurance companies should have the ability to classify as superannuation policies annuities sold to trustees of superannuation schemes¹⁰⁰.

⁹⁸ The Hancock Report 52 [4.19].

⁹⁹ Ibid 52 [4.20]-[4.21].

¹⁰⁰ Ibid ix, xv, 126-7 [8.14]-[8.18].

To protect members' entitlements, the Hancock Committee recommended:

1. vesting¹⁰¹ and preservation of members' benefits¹⁰²;
2. a fixed retirement age;¹⁰³
3. security of benefits;¹⁰⁴ and
4. disclosure and reporting.¹⁰⁵

6.2.4 The Campbell Report

The Campbell Committee was established in 1979 by the Federal Government to examine the Australian financial system and to recommend changes.¹⁰⁶ This Committee was to inquire into, and report on, regulation and control of the financial system and make recommendations for improvements in its structure and operations and control.¹⁰⁷ The Committee considered the analysis and conclusions of the Hancock Committee for a number of issues pertinent to its deliberations. It agreed with some recommendations and rejected others.¹⁰⁸

In its Report, superannuation funds were included in the review as private sector institutions. The Campbell Committee questioned the efficiency of the departure from tax neutrality adopted by the Federal Government to achieve their objective of encouraging long-term saving for retirement through formal superannuation

¹⁰¹ Ibid x-xi, 83 [6.5].

¹⁰² Ibid xi, 89 [6.21].

¹⁰³ Ibid xi, 93 [6.36]-[6.38].

¹⁰⁴ Ibid xii, 101-105 [7.2]-[7.17].

¹⁰⁵ Ibid xii, 105-106 [7.18]-[7.21].

¹⁰⁶ Edna Carew, *The Language of Money* (Allen & Unwin, 1988).

The Liberal-Country Party coalition government under Prime Minister the Rt Hon John Malcolm Fraser, AC CH created the Campbell Committee. That government lost an election in March 1983. On gaining office, the Hawke Labor government established the Martin Group to examine some of the findings of the Campbell Committee to ensure they reflected Labor's economic and social objectives.

Australian Bankers' Association Inc. *Fact sheets Selected events in the evolution of the Australian financial system*, 2004.

The Martin Committee endorsed the Campbell Report.

¹⁰⁷ Ibid.

¹⁰⁸ The Campbell Report 345 [20..97]-[20.101].

arrangements.¹⁰⁹ It also questioned the effect of government involvement in regulating the financial system when trying to protect investors.¹¹⁰

6.2.4.1 Prudential protection

The Campbell Committee made a number of observations about the protection of Members' benefits within the *ITAA*. The requirements of the *ITAA* and the trust deed together with the obligations and duties of the trustees of the state trustee legislation ostensibly protected members' benefits.¹¹¹ Members' benefits had additional protection if life insurance companies operated the superannuation fund. These superannuation funds were included in their statutory funds and came under the Life Insurance Act.¹¹²

For a superannuation fund to qualify for income tax concessions, the trustee had to ensure that the Commissioner of Taxation was satisfied that the superannuation fund complied with various discretionary tests. Tax avoidance and welfare objectives were the purpose of the provisions of the *ITAA*. Prudential considerations were of lesser importance.¹¹³

The trust deed of a superannuation fund usually provided the requirements for the administration of the fund. Whilst the power of the trustee was the subject of State trustee legislation, the trust deed commonly excluded the investment restrictions imposed by

¹⁰⁹ Ibid 245 [15.65].

¹¹⁰ Ibid 285-291 [18.7]-[18.49].

¹¹¹ Ibid 343 [20.91].

¹¹² Ibid 343 [20.91] n 19.

Members' interests are protected to the extent that the Life Commissioner can take certain action in the event that a life office is unlikely to meet its liabilities. However, individual funds included in a life office's statutory fund are not normally supervised by the Commissioner. While the Commissioner requires each life office to send him a list of 'benefit promise' funds it administers, together with the actuarially calculated contribution rate, he has no power to require that any such rate is in fact paid – i.e. he cannot ensure that funding arrangements are appropriate to the benefit promised. This is a matter for the fund trustees.

¹¹³ Ibid.

the state Trustee Acts¹¹⁴ and were usually drawn to give the trustee wide discretionary powers.¹¹⁵ The trustees were sometimes subject to direction by the employers on particular matters.¹¹⁶

The Campbell Committee referred to practices in other countries. The protection of employees' benefits did not rely on self-regulation by superannuation funds but imposed:

- (i) minimum requirements as a pre-condition for favourable tax treatment – with compliance supervised by the taxation authorities;
- (ii) tax-related requirements as in (i), but with compliance supervised by an independent authority; or
- (iii) prescribed minimum prudential standards (unrelated to the tax treatment of superannuation funds), compliance with those standards being by an independent authority.¹¹⁷

The Campbell Committee noted that members of Australian superannuation funds (other than non-unit-linked funds managed by life offices) had only minimum protection against possible diminution in value of accumulated funds. The trust deeds of most schemes permitted employers to discontinue contributions. The Campbell Committee noted that the security of benefits of superannuants was not a problem to date.¹¹⁸ This was contrary to other opinions¹¹⁹ and evidence.¹²⁰

The Campbell Committee did not advocate extending the scope of the Commissioner of Taxation's role to incorporate prudential, as

¹¹⁴ See Chapter 2 [2.1].

¹¹⁵ The Campbell Report 343-344 [20.91].

¹¹⁶ Ibid. *Mahoney v FC of T* (1965) 13 ATD 519, 525.

¹¹⁷ Ibid 344 [20.92].

¹¹⁸ The Campbell Report 345 [20.96].

¹¹⁹ The Asprey Report [21.101]; the Hancock Report 101-5 [7.2]-[7.17].

¹²⁰ *FC of T v The Northern Timber and Hardware Company Proprietary Limited* (1960) 103 CLR 650, 657; *Driclad Pty Ltd v FC of T* (1966) 121 CLR 45, 58-59; *Case U227 87 ATC* 1265, *Case X62 90 ATC* 469, 480.

opposed to revenue, considerations.¹²¹ Alternatives considered were:

- tax benefits should be subject to the registration or approval of superannuation funds having met prescribed prudential criteria by the Life Insurance Commissioner;¹²² or
- the Association of Superannuation Funds of Australia ('ASFA') be involved in actively developing minimum standards and monitoring their adequacy. The role for trustees could be continuing and possibly strengthened.¹²³

An issue of concern was the possible difficulties associated with the regulation of superannuation funds other than by way of the taxation power. The Campbell Committee favoured regulating by taxation power and the use of auditors to ensure minimum prudential standards were met.¹²⁴

The Committee recommended that:

- (a) Only contributions to an 'approved' superannuation fund should be rebateable (or deductible) for income tax purposes.
- (b) An 'approved' fund would be one that met certain minimum prudential requirements. These should be set (and reviewed regularly) by the Life Insurance Commissioner (who would *not*, however, have any ongoing supervisory responsibilities).
- (c) The requirements should be incorporated in the trust deeds of superannuation funds.
- (d) The auditor for each superannuation fund should provide the fund with a certificate each year confirming that the minimum requirements have been met.
- (e) The superannuation fund should lodge this certificate with its annual tax return; this would provide the basis for rebateability (or deductibility) of contributions.¹²⁵

¹²¹ Ibid 345-6 [20.100].

¹²² Ibid 345 [20.102].

¹²³ Ibid 345 [20.103].

¹²⁴ The Campbell Report 346 [20.105], 789 [45.150].

¹²⁵ Ibid 346 [20.107].

The Campbell Committee believed that these recommendations would:

- permit a reduced role for the Taxation Office in the oversight of observance of minimum prudential standards;
- make use of the experience and expertise of the Life Insurance Commissioner, but without adding to his ongoing supervisory responsibilities; in turn, this would ensure that regulation of all superannuation funds, including those operated by life offices, was on a consistent basis; and
- avoid a dispersion of regulatory responsibility between different government authorities.¹²⁶

The Campbell Committee observed that their recommendations did not differentiate between the different types of superannuation funds dependent on who made the contributions. It commented that whilst contributors to public funds were unlikely to be ‘at risk’, public superannuation funds should be required to comply with the same standards so that beneficiaries were treated equitably.¹²⁷ Public sector funds should in principle be treated for taxation purposes no differently from private sector funds.¹²⁸

The Campbell Committee recognised that prudential safeguards were less necessary where the owners or partners of the firm were the sole contributors and beneficiaries and the recommendations did not generally apply to such superannuation funds.¹²⁹

6.2.4.2 *Other protection*

The Campbell Committee recognised, as did the Hancock Committee,¹³⁰ that there were a number of distinct issues that

¹²⁶ Ibid 346-7 [20.108].

¹²⁷ Ibid 347 [20.109].

¹²⁸ Ibid 248-9 [15.85]-[15.88].

¹²⁹ Ibid 347 [20.109] n 27.

¹³⁰ The Hancock Report 9 [2.15], 17-18 [2.37]-[2.41], 102 [7.6], 104-5 [7.13]-[7.17], 105-6 [7.18]-[7.21].

needed to be addressed to provide protection in addition to that afforded by prudential supervision. These included:

- (a) employers' commitment and funding standards;¹³¹
- (b) asset restriction;¹³² and
- (c) disclosure and accountability.¹³³

- (a) Employers commitment and funding standards

- (i) *Compliance with actuarial recommendations*

Benefit promise schemes where the retirement benefit was related not to contributions but to pre-retirement salary should be subject to actuarial investigation from time to time with the actuary recommending a rate of contribution by the employer necessary to ensure that the accrued benefits were being fully funded. Funding the accrued benefits for members often was the responsibility of the trustee and subject to the terms and conditions of the relevant trust deed and sometimes the employer.

Rather than imposing conditions for compliance by the trustee of the superannuation fund in relation to adequacy of accrued benefits in benefit promise schemes advocated by the Hancock Committee,¹³⁴ the Campbell Committee favoured allowing the employer to determine the level of contribution and benefit for employees subject to compliance with the trust deed. The imposition of minimum funding standards on employers was likely to inhibit them from providing superannuation benefits, especially of the benefit promise kind.¹³⁵

¹³¹ The Campbell Report 347-8 [20.111]-[20.122].

¹³² Ibid 348-350 [20.123]-[20.130].

¹³³ Ibid 350-352 [20.131]-[20.144].

¹³⁴ The Hancock Report 102 [7.6].

¹³⁵ The Campbell Report 347-8 [20.115], 789 [45.151].

The Campbell Committee stated that it was essential that members were made aware of the level of funding by employers and the relationship of that funding to promised or indicated benefits. The Campbell Committee recommended that:

as a condition of qualification as an 'approved' fund, the trust deeds of superannuation schemes should require that members be kept regularly informed of the level of funding in relation to the obligations of employers under trust deeds.¹³⁶

(ii) Discontinuation of employer contributions

Where an employer discontinued their contributions to a benefit promise scheme, in many cases employers were not required to makeup any shortfall that existed at the time of discontinuance.¹³⁷ Where an employer chose to discontinue contributing to superannuation schemes, benefits associated with future service should be revocable but the same right should not apply to benefits accrued for previous service except where the trust deed allowed. The Campbell Committee recommended that:

benefits accrued in superannuation schemes in respect of previous services should not be revocable by the employer, except where the trust deed so provides.¹³⁸

(b) Asset Restrictions

The Campbell Committee was concerned that the security of members' benefits might be impaired if the value of any individual investment comprised an undue proportion of the assets of a superannuation fund. It recommended that, in order to qualify as an approved fund:

¹³⁶ Ibid 348 [20.117].

¹³⁷ The Hancock Report 103 [7.10].

¹³⁸ The Campbell Report 348 [20.188]-[20.122].

- (a) A superannuation fund (other than one administered by a life office or other pooled fund) should be required to restrict its investment in any single asset to not more than 5% of the total assets of the fund, both values to be current market values. A pooled fund should be required to observe the same constraint in respect of its overall portfolio.
- (b) Where the value of an individual investment exceeds this figure (arising, for example, from the revaluation of an asset or a change in the market valuation of an investment), the fund should be permitted twelve months to reduce its holding to the 5% level.
- (c) Where any fund's investment exceed the 5% limit at the time these arrangements are implemented, a transitional period of three years should be permitted.¹³⁹

A further concern was the security of members' benefits being seriously impaired in the absence of specific limitations in the employer's business. It was argued that:

- if the company fails, the employee could lose their superannuation benefits as well as their jobs;
- the investment may not be at 'arm's length';
- the dominant motive for establishing and maintaining the relevant schemes may be to reduce the company's taxation and improve its liquidity rather than to provide benefits to the company's employees upon retirement.¹⁴⁰

The Campbell Committee recommended that:

- in general, not more than 5% of the assets of a superannuation fund should consist of an investment (equity and/or loans) in the employer's business;¹⁴¹
- to enable employers to rearrange their financing, a longer transitional period should be permitted, before the 5% ceiling

¹³⁹ Ibid 349 [20.125], 789 [45.152].

¹⁴⁰ Ibid 349 [20.126].

¹⁴¹ Ibid 350 [20.128], 789-90 [45.152].

is applied, than is proposed in respect of other investments.¹⁴²

(c) Disclosure and Accountability

(i) *Reporting Requirements*

The Campbell Committee accepted that there was a need for improved disclosure to members of superannuation funds. It recommended the adoption of the reporting standards advocated by the ASFA as a condition of qualification as an ‘approved’ fund. ASFA had published minimum reporting standards for superannuation funds.¹⁴³ These standards required that:

- the annual report of a superannuation scheme should comprise reports by the trustees and the actuary (where appropriate) as well as financial accounts and an auditor’s report;
- members should be provided with an abbreviated report containing information on the financial position of the scheme expressed in a simple and straightforward manner; the report should include a table of investments of various types, at market value; and
- members should have access to a copy of the full report if they wish, and be provided annually with a statement of accumulated contributions and benefits.¹⁴⁴

(ii) *Participation of Members*

The Campbell Committee recommended that a condition of qualification as an ‘approved’ fund should be that the trust deed provide for the annual election of at least one representative of non-management employee members as a trustee of the fund. This appointment was expected to

¹⁴² Ibid 350 [20.130], 790 [45.152].

¹⁴³ Ibid 351 [20.139], 790 [45.154].

¹⁴⁴ Ibid 351 [20.137], *Superannuation Scheme Practice and Reporting in Australian*, the Association of Superannuation Funds of Australia, Booklet No 10 December 1979.

minimise potential conflicts of interest and strengthen the independence of trustees. In addition, it was expected that the superannuation fund would be administered more clearly in the interest of members and there would be an improvement in communications between scheme administrators and members.¹⁴⁵

In summary, for purposes of regulation of superannuation funds and protection of members' benefits, the Campbell Committee recommended that:

1. a superannuation fund be an 'approved' superannuation fund which met certain minimum requirements;¹⁴⁶
2. the minimum prudential requirements be incorporated in the trust deeds of the superannuation fund;¹⁴⁷
3. an auditor certify that the superannuation fund met the minimum requirements each year;¹⁴⁸
4. tax concessions depend on the superannuation fund lodging the auditor's confirmation of compliance with the minimum standards;¹⁴⁹
5. the trust deed require members to be kept regularly informed of the level of funding in relation to the obligations of employers under the trust deed;¹⁵⁰
6. accrued benefits not be revocable by an employer, except where the trust deed provides;¹⁵¹
7. investment in a single asset be restricted to 5% of the total assets of the fund at current market values for superannuation funds, except those administered by a life

¹⁴⁵ Ibid 352 [20.140]-[20.144], 790 [45.154].

¹⁴⁶ Ibid 346 [20.107].

¹⁴⁷ Ibid.

¹⁴⁸ Ibid.

¹⁴⁹ Ibid.

¹⁵⁰ Ibid 348 [20.117].

¹⁵¹ Ibid [20.122].

- office or other pooled fund. If this occurred, twelve months be allowed to reverse this position;¹⁵²
8. investment (equity and/or loans) of not more than 5% of the assets of a superannuation fund in the employer's business be allowed;¹⁵³
 9. reporting standards be a condition of qualification as an 'approved' fund;¹⁵⁴
 10. the election of at least one representative on non-management employee-members be a condition of qualification as an 'approved' fund.¹⁵⁵

6.2.5 The Task Force Report

In 1979, the Treasurer of the Federal Government¹⁵⁶ announced¹⁵⁷ the establishment of a Task Force:

to consider the role of occupational superannuation in providing for retirement and to determine whether there was a need to revise or impose new standards for superannuation schemes.¹⁵⁸

The Federal Government referred the Task Force to the views expressed by the Hancock Committee¹⁵⁹. As well as consulting various organisations¹⁶⁰ actively engaged in the superannuation area, the Task Force took the Reports of previous Committees¹⁶¹ and their recommendations into account when deliberating about

¹⁵² Ibid 349 [20.125].

¹⁵³ Ibid 350 [20.128].

¹⁵⁴ Ibid 351 [20.139].

¹⁵⁵ Ibid 352 [20.144].

¹⁵⁶ Liberal-Country Party coalition government under the Prime Minister the Rt Hon John Malcolm Fraser, AC, CH.

¹⁵⁷ The Treasurer, the Hon John Howard, MP, 'Superannuation', Press Release No 68, 12 July 1979.

¹⁵⁸ Ibid.

¹⁵⁹ The Task Force Report 3 [1.2].

¹⁶⁰ Ibid 5 [1.15]. Life Insurance Federation of Australia, the Association of Superannuation Funds of Australia, the Association of Consulting Actuaries, Australian Government Actuary.

¹⁶¹ The Asprey Committee, the Campbell Committee, the Hancock Committee.

its conclusions and recommendations.¹⁶² A number of recommendations of the previous Committees were adopted by the Task Force.

The Task Force considered in its deliberations policy issues connected with superannuation and its interaction with social security and taxation policies.¹⁶³ The policy issues included matters relating to the encouragement of arrangements directed at genuine provisions for retirement, the development of improved operational standards and the demand for annuities.¹⁶⁴

The Federal Government specifically requested that the Task Force consider the possible vesting, preservation and portability arrangements as well as improving prudential standards.¹⁶⁵ The Task Force was to address the question of using annuities to provide for retirement.¹⁶⁶ In its deliberations, it recognised the need to strike a balance between protecting the interests of members whilst avoiding undue government intervention and regulation of activities, bearing in mind the tax concessions associated with superannuation transactions.¹⁶⁷

The Treasurer and the Minister for Industrial Affairs in a joint press release¹⁶⁸ of 6 September 1979 confirmed the Federal Government's commitment to encouraging people to save for their retirement by stating that it was:

concerned to ensure that superannuation arrangements are not used for purposes other than genuine retirement such as the cash payment of an

¹⁶² The Task Force Report 3 [1.5]-[1.6].

¹⁶³ Ibid 4 [1.8(a)], [1.9].

¹⁶⁴ Ibid 4 [1.8(b)].

¹⁶⁵ Ibid 5 [1.10].

¹⁶⁶ Ibid.

¹⁶⁷ Ibid 5-6 [1.16].

¹⁶⁸ The Treasurer, the Hon John Howard MP and Minister for Industrial Relations, the Hon Tony Street MP, 'Occupational Superannuation', Press Release, No 90, 6 September 1979.

employer's contributions to an employee who chooses to change employment after a relatively short period of service.¹⁶⁹

The issues on which the Task Force made recommendations were:

1. vesting and preservation;¹⁷⁰
2. security of superannuation benefits;¹⁷¹ and
3. the demand for annuities.¹⁷²

The Task Force considered the differences that might exist between private sector schemes and public sector schemes. It concluded that, as a general rule, the same proposed standards should apply to both types of funds.¹⁷³ The differences were such that implementation of some of the proposed prudential standards was not required. Public sector funds were not subject to the same controls and restrictions that applied in the *ITAA*. Members' benefits were generally subject to government financial backing.¹⁷⁴ Other proposed standards were considered applicable to public sector schemes and provided protection.¹⁷⁵

6.2.5.1 *Vesting and preservation*

The Task Force defined 'vesting' as relating to 'the employee's entitlement to benefits accrued within a fund up to the date of his withdrawal from the service of the employer.'¹⁷⁶ It defined 'preservation' as referring to:

the vested amount not being distributed at the time of termination of employment but being preserved, together with any accrual to the

¹⁶⁹ The Task Force Report 14 [3.7].

¹⁷⁰ Ibid 13-29 [3.1]-[3.73].

¹⁷¹ Ibid 31-41 [4.1]-[4.50].

¹⁷² Ibid 42-48 [5.1]-[5.32].

¹⁷³ Ibid 6 [1.17].

¹⁷⁴ Ibid 6 [1.17], 31 [4.6].

¹⁷⁵ See [6.2.5.1].

¹⁷⁶ The Task Force Report 13 [3.2].

preserved amount, until final retirement, death or until other special circumstances arise.¹⁷⁷

In the absence of readily available machinery, including transferability of members' benefits to new employers, vested benefits were, in most cases, paid out in cash to the employee.¹⁷⁸

The Task Force identified the essence of vesting and preservation of members' benefits as ensuring that the accrued superannuation benefits of an employee:

1. were not distributed at the time of termination of employment but preserved with any earnings of the accrued amount until final retirement, death or until other special circumstances;¹⁷⁹ and
2. were not lost when the employee changed employment but were to be carried over in an appropriate manner for use in genuine retirement.¹⁸⁰

The Task Force considered that compulsory vesting, preservation and portability of members' benefit would:

1. result in employees, particularly those in the higher age bracket, not being prohibited from changing employment because the forgoing of their superannuation benefits might represent a substantial loss. Preservation of members' entitlement would aid the mobility of labour;¹⁸¹ and
2. prevent arrangements which used the superannuation medium as a means of providing largely tax-free deferred pay to employees on termination of employment.¹⁸²

¹⁷⁷ Ibid [3.3].

¹⁷⁸ Ibid 14 [3.10].

¹⁷⁹ Ibid 13 [3.3].

¹⁸⁰ Ibid 13 [3.1].

¹⁸¹ Ibid 15 [3.12].

¹⁸² Ibid 15 [3.13].

The provisions of the *ITAA* under review by the Task Force did not require the trustee of a superannuation fund to vest any of the employer's contributions for the benefit of employees who terminated their employment either by choice or compulsion prior to retirement.¹⁸³ Proposed changes to the *ITAA* would include as a condition of approval for superannuation schemes vesting and preservation of retirement benefits in accordance with minimum prescribed standards.¹⁸⁴ The proposed minimum standards would differ for different types of superannuation schemes.¹⁸⁵

The Task Force recognised that the proposals for compulsory vesting and preserving of members' entitlements might result in negative attitudes by both employers and employees. For employers, there were two factors: the cost of possible increased contributions and administration and maintenance of members' entitlements.¹⁸⁶ For employees, non-availability of cash on withdrawal from occupational superannuation schemes represented a substantial loss that might not be recompensed by other parts of their employment package.¹⁸⁷

Employees' contributions, or equity in them, should vest in full.¹⁸⁸ Employers' contributions should have minimum prescribed bases. These should include principles that might depend on contributions, age and period of service restrictions with different formulae applied to the different types of superannuation schemes.¹⁸⁹ Vested amounts should be preserved until genuine

¹⁸³ Ibid 13[3.2].

¹⁸⁴ Ibid 7 [2.3], 19-24 [3.30]-[3.52].

¹⁸⁵ Ibid 7 [2.6], 17-24 [3.25]-[3.52]. These schemes included allocated cash accumulation type schemes, allocated endowment schemes, unallocated defined benefit schemes, pension schemes.

¹⁸⁶ Ibid 16 [3.17]-[3.19].

¹⁸⁷ Ibid 16 [3.20].

¹⁸⁸ Ibid 7 [2.4].

¹⁸⁹ Ibid 7 [2.6], 17-23 [3.25]-[3.52].

retirement.¹⁹⁰ The application of the provisions prior to the introduction of the proposals should continue to apply to contributions previously made.¹⁹¹

Preservation of a member's vested entitlement could be in the original employer's superannuation fund, the new employer's superannuation fund, or if the employee so elected, placed 'with some other appropriate party'.¹⁹² The Task Force came to the conclusion that freedom of choice with regard to placement of preserved benefits should apply without exception.¹⁹³

Members' entitlements retained in an employer's superannuation fund should be dealt with in accordance with the rules of those superannuation funds.¹⁹⁴

Members' entitlements transferred to a new employer's superannuation fund should depend on the type of scheme of the new employer. If the new employer's superannuation fund was of the accumulation type, the terms of the scheme should apply to the transferred members' entitlements. If the superannuation scheme was an unallocated defined benefit scheme, the method of treating the new member's entitlement should be dealt with in a way that was considered fair by the employee and the new employer and in accordance with the rules of the new superannuation fund. An actuary could determine what was fair and equitable.¹⁹⁵

¹⁹⁰ Ibid 8 [2.9], 15 [3.14].

¹⁹¹ Ibid 7 [2.4], 23 [3.50].

¹⁹² Ibid 13 [3.4], 25-27 [3.58]-[3.66].

¹⁹³ Ibid 27 [3.67].

¹⁹⁴ Ibid 8 [2.9], 26 [3.62].

¹⁹⁵ Ibid 27 [3.64]-[3.65].

It was suggested that the same requirements for vesting and preservation apply to both public sector schemes and private sector schemes.¹⁹⁶

Where a member elected to use an approved deposit fund for benefits, the amount transferred from superannuation funds should be paid directly into approved deposit funds (ie not through the member) and accumulate interest until withdrawal at prescribed times.¹⁹⁷ The requirements for compliance by approved deposit funds should be similar to those applying to life insurance companies.¹⁹⁸ These rules should include an obligation:

- (i) to clearly state the terms on which the money is to be managed;
- (ii) to operate the business under the provisions of a Trust Deed similar to that required by superannuation funds;
- (iii) to comply with the supervisory standards at least comparable to those applicable to life offices and with any requirements placed on superannuation funds regarding the investment of the assets; and
- (iv) to establish adequate machinery to check that a benefit is eligible for payment eg that the retirement age has been reached or that proof of death is satisfactory.¹⁹⁹

The trustees of approved deposit funds should be required to satisfy the requirements for exemption on investment income.²⁰⁰

The similar standards of security, reporting and disclosure should apply to approved deposit funds as applied to superannuation funds.²⁰¹

For the Federal Government, the cost to the Revenue of compulsory vesting and preservation of members' benefits related to the cost of providing entitlements for its own staff. Also to be

¹⁹⁶ Ibid 9 [2.12], 27 [3.67].

¹⁹⁷ Ibid 8 [2.9].

¹⁹⁸ Ibid 9 [2.10].

¹⁹⁹ Ibid 26 [3.60].

²⁰⁰ Ibid 9 [2.11], 27 [3.66].

²⁰¹ Ibid 9 [2.11].

taken into consideration was the possible cost of additional tax deductions for the additional contributions by employers and the additional tax exemption or concessional treatment of income of superannuation funds.²⁰² The Task Force considered that the net effect in the long term could be of substantial importance. The precise effect would depend on participation in occupational superannuation, the social and economic benefits of this participation and the taxation treatment of benefits.²⁰³

The vesting and preservation proposals were developed to reinforce the Federal Government's policy to encourage savings for genuine retirement purposes.²⁰⁴ The Task Force believed that a system of vesting and preservation arrangements would be fully consistent with the Federal Government's objective and policy intent of encouraging people to save for their own retirement by protecting their benefits. Significant tax advantages were to continue to be given to superannuation funds mainly because of their specific role in providing retirement, death and disability benefits. Unless members' benefits were preserved for retirement, the rationale for providing the exemption and tax concessions could not be supported.²⁰⁵

6.2.5.2 Security of Superannuation Benefits

Having confirmed the necessity of vesting and preservation of members' benefits, proposals were developed to further protect members' benefits. Restricting investment by a superannuation fund in an employer's business was considered important on the basis that:

- at the time a member retires the trustee of a superannuation fund that had invested in the contributing employer might

²⁰² Ibid 24 [3.54].

²⁰³ Ibid 25 [3.54]-[3.55].

²⁰⁴ Ibid 7 [2.2].

²⁰⁵ Ibid 15 [3.14].

have difficulty in providing cash to finance the member's benefits;

- if the employer's business fails, the employees could lose their superannuation benefits as well as their jobs;
- the motive of contributing by an employer to a superannuation fund for an allowable deduction and investing the contribution back into that employer for liquidity purposes would be minimised;
- loan back arrangements by the trustee of a superannuation fund to an employer might be inconsistent with the duty under the law for the trustee of the superannuation fund to act prudently and for the benefit of the members of the fund.²⁰⁶

The Task Force identified the lack of prudential supervision in the superannuation industry at either a Commonwealth or State Government level. Protection of members' benefits depended on compliance by the trustees with trust instruments and on arrangements for a fund to qualify for income tax concessions subject to meeting the discretionary tests imposed by the Commissioner of Taxation.²⁰⁷ The Task Force considered the possibility of imposing penalties on trustees for non-compliance with the proposed standards. It decided that in the event of the trustees' failure to comply with standards, the loss by the superannuation fund of its concessional taxation status would be a sufficient penalty. It did not feel that it would be productive or in the interests of employees to impose penalties on trustees for non-compliance additional to those provided under trustee legislation. To the extent that trustees were in breach of the terms of the trust

²⁰⁶ Ibid 37-8 [4.32]-[4.39].

²⁰⁷ Ibid 30 [4.3]. These tests were designed primarily for the protection of the Revenue.

deed, members of a superannuation fund could consider initiating legal proceedings against the trustee.²⁰⁸

The Task Force noted the comments in the Hancock Committee Report²⁰⁹ and the Campbell Report²¹⁰ as to the powers of the Commonwealth under the *Constitution* to legislate on prudential aspects of superannuation funds.²¹¹ These Reports identified the taxation power of the *Constitution* as being the main and more certain legislative authority.

The Task Force recognised a number of considerations as important in formulating the prudential regulation of superannuation funds. These included the following:

- whether it was appropriate that the Taxation Commissioner, whose primary function is the collection of revenue, should also be charged with the responsibility for the prudential oversight of superannuation funds;
- notwithstanding the first point, the undoubted expertise of the Taxation Office in relation to superannuation fund arrangements should be recognised and utilized where possible;
- it would be sensible to draw upon the existing expertise of the Life Insurance Commissioner in his role of prudential oversight of life insurance companies, especially in relation to their superannuation business;
- there should be avoidance of any unnecessary duplication of the bureaucracy that might be associated with the establishment of additional supervisory machinery to oversight the activities of funds;
- the extent to which any supervisory arrangements which might be developed might be supplementary to existing trustee law;
- the scope that might exist for restricting the degree of Government involvement in supervision by implementing arrangements which

208 Ibid 32 [4.9]-[4.10].

209 The Hancock Report 51-52 [4.19]-[4.21].

210 The Campbell Report 346 [20.105], 789 [45.150].

211 The Task Force Report 30 [4.4].

place greater reliance on private professional and technical expertise eg that of actuaries, auditors, etc;

- the extent to which greater disclosure of information to fund members on their rights and the operations of funds might be an appropriate alternative to greater regulation;
- the extent to which participation by employees in the management of superannuation funds should be encouraged.²¹²

To access taxation concessions allowed by the *ITAA*, the trustee of a superannuation fund should ensure that the superannuation fund complied with the provisions relating to the security of members' benefits. These requirements would include restricting:

- amendments to the trust deed for the superannuation fund to reduce entitlements accrued to members prior to any amendment;²¹³
- subject to transitional arrangements, investment by an employer-sponsored superannuation fund. Equities in, or loans to, the employer's business, a related company or associated persons would be restricted to no more than 10 per cent of the assets of the superannuation fund, measured at cost. The Task Force proposed no other restrictions on investment by the trustee of a superannuation fund;²¹⁴
- any charge on assets of the superannuation fund except to obtain temporary funds²¹⁵.

Member representation in the management of superannuation funds was also to be encouraged. This might be effective in safeguarding members' benefits but would depend on the 'financial expertise of their representatives and on the extent to which

²¹² Ibid 30-1 [4.5].

²¹³ Ibid 9 [2.15], 35 [4.22].

²¹⁴ Ibid 9-10 [2.16]-[2.18], 37 [4.35].

²¹⁵ Ibid 10 [2.19], 41 [4.47].

members themselves monitored the fund's activities to ensure that the trustees were managing the fund in their interests.²¹⁶

Reporting and disclosure of information were identified as preferable to imposing additional compliance requirements and could serve as a substitute for regulation.²¹⁷ Regular disclosure of certain information to members of superannuation funds should be a requirement. This would include:

- (i) providing information on prospective entitlements to members at the time of their joining the fund;
- (ii) making available to a member on request:
 - (a) information relating to that member's expected retirement benefits and current benefit entitlement, if any, together with the amount of that member's contributions to the fund to date; and
 - (b) an audited statement of net assets (indicating the basis of calculation used) and income and expenditure accounts with a related audit certificate. These financial statements were to be audited annually and prepared in accordance with recommendations by ASFA.²¹⁸

Annual reporting to members would include confirmation of compliance with the requirements relating to the protection of members' entitlements.²¹⁹ Reporting and disclosure by the trustee of a superannuation fund would allow members and other interested parties to review this information. This requirement would have the effect of making trustees more conscious of their legal obligations to members under the general law relating to trusts.

²¹⁶ Ibid 10 [2.20], 41 [4.49].

²¹⁷ Ibid 38 [4.40], the Campbell Report 350 [20.131].

²¹⁸ The Task Force Report 10 [2.22], 39 [4.44].

²¹⁹ Ibid 10-11 [2.23], 39 [4.44].

Members must be made aware that a superannuation fund that has secured approval under the *ITAA* should not be regarded as a guarantee of financial strength given the wide range of financial standards to be observed within the superannuation industry.²²⁰

6.2.5.3 *Demand for Annuities*

The Federal Government asked the Task Force to consider the use of annuities in providing for retirement.²²¹ The Task Force defined an annuity as ‘a contract whereby a purchaser is provided with a regular income for a specified period of time, such as a number of years or for life, by a seller (usually a life office). The regular income flow comprises both the return of the capital used to purchase the annuity and an interest component.’²²² It identified two types of annuities:

- an immediate annuity, which is purchased by a single payment, with the first payment to the purchaser being delayed no longer than the regular interval between subsequent payments; and
- a deferred annuity, where there is a delay between the time that the first (or single) premium is paid and the time that the first payment is received (e.g. premiums are paid during a person’s working life to purchase a deferred annuity which commences payment at age 65).²²³

For individuals in retirement, annuities would provide regular and certain flow of income. For the trustees of occupational superannuation funds, they would provide a greater flexibility and choice in arrangements for retirement planning.²²⁴

To make annuities attractive to market, certain restraints should be removed. These would include:

- removal of the double taxation treatment of the income

²²⁰ Ibid 11 [2.25].

²²¹ Ibid 5 [1.10].

²²² Ibid 42 [5.2].

²²³ Ibid 42 [5.3].

²²⁴ Ibid 11 [2.26].

component;²²⁵ and

- amendment of the minimum valuation basis prescribed in the *Life Insurance Act* as it related to annuities.²²⁶

The Task Force referred to, analysed and considered the conclusions of the Hancock and Campbell Reports. By doing this, it determined that there was a need to impose new standards for superannuation schemes. The new proposed standards related to the regulation of superannuation funds. They supported the Federal Government's policy intent to encourage persons to save for their retirement by ensuring that members would know what benefits they were entitled to before and after retirement. The measures recommended were to secure these benefits and ensure they would be available at retirement.

In summary, the Task Force proposed the following as a framework for the prudential supervision of superannuation funds:

- each superannuation fund would be required to meet certain minimum prudential standards set (and reviewed regularly) by the Treasurer in consultation with the Life Insurance Commissioner, who would not, however, have any on-going supervisory responsibilities;
- each fund would be audited annually, with the auditor providing the trustee with a certificate confirming that the prudential standards had been met. (There may be a need, however, to allow for the audit requirement to be dispensed with in certain circumstances eg in relation to a very small superannuation fund comprising only, say, three employees where there is close relationship between all the interests involved.);
- this certificate would be lodged with a fund's annual taxation return and would form part of the information available to members on request;
- those funds which failed to comply with these standards would lose their favoured taxation status for that year (but consideration

²²⁵ Ibid 11 [2.27], 44-46 [5.14]-[5.22].

²²⁶ Ibid 11 [2.27], 46-47 [5.23]-[5.26].

- should be given to allowing the Commissioner a discretion to disregard some temporary non-compliance of a minor nature);
- public sector schemes would be encouraged to observe standards which are at least the broad equivalent of those being proposed, except that to the extent that such funds are guaranteed, prudential controls (over such matters as investment practices) would not be necessary; and
 - funds would be required to meet certain standards of disclosure and reporting.²²⁷

For the protection of members' benefits, the Task Force recommended:

1. vesting²²⁸ and preservation of members' benefits in accordance with minimum prescribed standards;²²⁹
2. restricted investment (equity or loans) in employers' businesses;²³⁰
3. prohibition on charging assets of the superannuation fund except to obtain temporary finance;²³¹
4. member representation in the management of the fund;²³²
5. disclosure of information and annual reporting;²³³
6. amendment of legislation (*ITAA* and *Life Insurance Act*) to allow annuities to be offered as an alternative tax and cost

²²⁷ Ibid 32-3 [4.11].

²²⁸ The Task Force 7-12 [2.1]-[2.29], 13-29 [3.1]-[3.74].
Referred to in: the Asprey Report [21.111], [21.114], [21.119], [21.131]; the Hancock Report 82-8 [6.4]-[6.20].

²²⁹ The Task Force 7-12 [2.1]-[2.29], 13-29 [3.1]-[3.74].
Referred to in: the Asprey Report [21.96(b)]; the Hancock Report 89-93 [6.21]-[6.35].

²³⁰ The Task Force 9-10 [2.16]-[2.17], 36-8 [4.30]-[4.39].
Referred to in: the Asprey Report [21.101]; the Hancock Report 101-5 [7.2]-[7.17]; the Campbell Report 348-350 [20.123]-[20.130].

²³¹ The Task Force 10 [2.19], 41 [4.47].

²³² The Task Force 10 [2.20]; 41 [4.48].
Referred to in: the Campbell Report 352 [20.140]-[20.144].

²³³ The Task Force 10 [2.22]-[2.23], 38-40 [4.40]-[4.45].
Referred to in: the Asprey Report [21.78], [21.143]; the Hancock Report xii, 105-6 [7.18]-[7.21]; the Campbell Report 350-351 [20.132]-[20.139].

effective investment to provide a regular and certain cash flow.²³⁴

6.3 Federal Government's Response

The Federal Government accepted and adopted the recommendations in the Task Force's Report. As directed, the Task Force had relied on the Hancock Report. In addition, it referred to the analyses in the Asprey Report and the Campbell Report. The Federal Government also incorporated recommendations from Reports in the OSSA and OSSR other than those in the Task Force's Report.

The Federal Government acknowledged the deficiencies in the existing occupational superannuation arrangements portrayed by the Committees. These deficiencies included the extent of coverage and the subsequent access to taxation benefits for retirement saving, the portability of superannuation benefits and the conditions relating to the vesting of employer contributions.²³⁵

In 1984, as part of the retirement policy developed to encourage employees to save for their retirement by using tax incentives and to assist the preservation of members' entitlements,²³⁶ the Federal Government introduced Approved Deposit Funds ('ADF').²³⁷ These were investment vehicles that provided a tax effective fund for the recipient of an eligible termination payment²³⁸ on changing

²³⁴ The Task Force 11-12 [2.26]-[2.29], 42-8 [5.1]-[5.32].
Referred to in: the Hancock Report 106-8 [7.22]-[7.25].
The Task Force 7-12 [2.1]-[2.29].

²³⁵ The Minister for Housing and Construction and Minister Assisting the Treasurer, the Hon Chris Hurford MP, 'Income Tax Assessment Amendment Act (No 3) 1984' (Second Reading Speech delivered at the House of Representatives, Canberra, 5 June 1984).

²³⁶ See above n 7.

²³⁷ ITAA ss 27A-27J, s 23FA, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 of 1984 applicable to assessments for the year of income commencing 1 July 1983 and all subsequent years.

²³⁸ ITAA s 27A included as an approved purpose the receiving on deposit amounts deemed by ITAA s 27D as eligible termination payments which qualify as able to be rolled over into ADFs.

employment.²³⁹ Employees who changed jobs were able to, without paying any tax, deposit any superannuation lump sum received on termination into an ADF. The structure of an ADF also introduced the concept of an independent trustee for a fund established for superannuation purposes in the *ITAA*.²⁴⁰

As part of these new rules for taxing superannuation and other retirement payments introduced in 1984²⁴¹, the Federal Government complied with the recommendations of the Task Force to improve the attractiveness of annuities, in particular the double taxation treatment of the income component of annuities.²⁴² It extended the definition of an eligible policy to include ‘immediate annuity’ and a ‘roll-over annuity’.²⁴³

After considering Reports received from Committees appointed to review the regulation of the superannuation industry, the Federal Government determined that the structure for regulation of superannuation funds and approved deposit funds had to be revised. The Treasurer, in his Press releases of June 11 and December 22 1986²⁴⁴ announced various operating standards which superannuation funds and approved deposit funds would be required to meet in order to be eligible for tax concessions.

²³⁹ *ITAA* pt III, div 2 sub-div AA - Superannuation, termination of employment and kindred payments, ss 27A-27J, as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 47 1984.

²⁴⁰ *ITAA* s 23FA(1). *ITAA* s 27A(1) (definition of ‘approved trustee’).

²⁴¹ *ITAA* 110(1) (definition of ‘eligible policy’), as inserted by *Income Tax Assessment Amendment Act (No 3) 1984*, No 49 of 1984. Applicable for 1983-1984 onwards.

²⁴² Task Force Report 11 [2.27]; 44 [5.4]-5.22].

²⁴³ *ITAA* s 27H(4) (definition of ‘annuity’ as ‘a superannuation pension’).
ITAA s 110 (definition of ‘immediate annuity’ to mean ‘an annuity that is presently payable to a natural person’); (definition of ‘roll-over annuity’ to mean ‘a deferred annuity the purchase price of which consists wholly of a rolled-over amount or rolled-over amounts’).
ITAA s 27A(1) (definition of ‘rolled-over amount’ to mean ‘so much of an eligible termination payment deemed by the application of s 27D to have been applied in payment of any part of the purchase price’).

²⁴⁴ The Treasurer, the Hon P J Keating MP ‘Occupational Standards for Occupational Superannuation Funds’ Press Release No 48, 11 June 1986; Press Release No 144, 22 December 1986.

In 1987, the Federal Government established standards following consultations with various interested groups and against the background of the Federal Government's concern to ensure that superannuation arrangements were directed at meeting genuine retirement needs and that members' entitlements were protected. The new legislation was 'to provide operating standards for certain superannuation funds and approved deposit funds, and for related purposes'²⁴⁵. This legislation was the O SSA and the O SSR. The Governor-General of the Commonwealth of Australia was allowed to make regulations, not inconsistent with the O SSA, during the period that the O SSA regulated funds.²⁴⁶

A new authority, the Insurance and Superannuation Commission ('ISC'), was established to regulate inter alia superannuation funds and ADFs and headed by the Insurance and Superannuation Commissioner. The Commissioner of Taxation retained the tax assessment role in relation to these funds. With the introduction of O SSA, the Federal Government levied an annual fee to recover the costs of administering the supervisory arrangements so that there would not be any net cost to the Revenue.²⁴⁷

As part of the new arrangements for the taxation of superannuation funds and ADFs introduced in 1988, the Federal Government introduced a new type of fund, 'Pooled Superannuation Trust' ('PST') to act as investment vehicles for complying superannuation and approved deposit funds.²⁴⁸ A PST

²⁴⁵ Introduction statement to the O SSA.

²⁴⁶ O SSA s 22.

²⁴⁷ O SSR reg 25, initially referring to O SSA ss 12, 14. O SSR reg 25 later amended by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1989 No 356, 7 December 1989 to include O SSA s 15B(1)(a)(iv), as inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989.

²⁴⁸ ITAA div 7 ss 296-299; O SSA s 3(1) (definition of 'pooled superannuation trust'); s 15B, as inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 7 1989 applicable to assessments for the year of income in which 1 July 1988 occurred and all subsequent years; O SSR reg 23A, as inserted by Commonwealth of Australia, *Occupational*

was defined in a similar way to a complying superannuation fund.²⁴⁹

The new method of regulating superannuation funds and ADFs and the innovative PSTs combined to support the Federal Government's retirement policy to encourage people to save for retirement. These new arrangements also demonstrated the Federal Government's intent to protect members' benefits.

6.4 Prudential Supervision

In 1986, the Treasurer announced the Federal Government's decision to establish a new body called the Insurance and Superannuation Commission ('ISC') to be headed by the Insurance and Superannuation Commissioner, a new statutory officer.²⁵⁰ The ISC brought together the existing Offices of Insurance Commission, Life Insurance Commissioner and Australian Government Actuary and included the proposed office relating to occupational superannuation.²⁵¹

When established, the ISC would regulate the administration and operations of superannuation funds and ADFs, ie the non-revenue superannuation requirements.²⁵² The Commissioner of Taxation would retain the tax assessment role in relation to these funds. This assessing role applied also to non-approved funds. The Commissioner of Taxation would also retain the responsibility for:

Superannuation Standards Regulations (Amendment), Statutory Rules 1989 No 356, 1 July 1988.

²⁴⁹ ITAA s 267(1).

²⁵⁰ The Treasurer, the Hon P J Keating MP 'Occupational Standards for Occupational Superannuation Funds' Press Release No 48, 11 June 1986; Press Release No 144, 22 December 1986.

²⁵¹ The Treasurer, the Hon P J Keating M P 'Occupational Standards for Occupational Superannuation Funds' Press Release No 48, 11 June 1986.
Three Bills to give effect to these announcements were introduced: *Occupational Superannuation Standards Bill 1987*, No 97 1987; *Insurance and Superannuation Commissioner Bill 1987*, No 98 1987; *Insurance and Superannuation Commissioner (Consequential Provisions) Bill 1987*, No 99 1987.

²⁵² OSSA s 9.

- allowing deductions for contributions to approved funds and certain non-approved funds in certain circumstances;²⁵³
- assessing payments by superannuation funds to members;²⁵⁴, and
- any excessive or unauthorised benefits paid to fund members or other persons.²⁵⁵

The basic objective of establishing the ISC was to achieve improved efficiency and co-ordination through the integration of the Commonwealth's various insurance, superannuation and actuarial functions. The Federal Government considered the establishment of the ISC and implementation of the O SSA as important elements in its overall retirement incomes policy.²⁵⁶ The detailed operating standards were included in the OSSR. These standards included the requirements for the protection of members' entitlements - vesting, preservation and portability of the members' entitlements, trustees and their appointment, investments, financial reports and disclosure, actuarial investigation and audits.

O SSA and OSSR commenced on 21 December 1987 but a number of provisions were deemed to have applied from 1 July 1986. From this time, federal legislation governed the taxation and operation of private sector superannuation funds. O SSA and OSSR applied to public sector funds from 1 July 1990.²⁵⁷

253 ITAA pt III div 3 sub-div AA – contributions to superannuation funds for Benefit of Employees.
ITAA pt III div 3 sub-div AB – contributions to superannuation funds by eligible persons.

254 ITAA pt III div 2 sub-div AA.

255 ITAA ss 26AF, 26AFA, 26AFB.

256 See above n 235.

257 Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, No 150, 25 June 1990.
OSSR reg 3C, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 275, 21 August 1990, to allow an order under the *Crimes (Superannuation Benefits) Act 1989* to be enforced against an employee of the Commonwealth convicted of a corruption offence committed while employed by the Commonwealth.

6.5 Requirements for Tax Relief

For exemption or the application of concessional rates of tax, the trustees of superannuation funds, ADFs and PSTs had to ensure compliance with the regulating provisions. There were two distinct periods during the time when the OSSA regulated these funds.

During the first period, the *ITAA* exempted the income of superannuation funds and ADFs from income tax provided they complied with the relevant provisions in the *ITAA*. This period ended 30 June 1988.

The second period of taxation of superannuation funds, ADFs and PSTs commenced 1 July 1988.²⁵⁸ It related to the introduction of the application of concessional rates of tax to their assessable income,²⁵⁹ including taxable contributions made to the fund²⁶⁰. Capital gains tax also applied to superannuation funds from 1 July 1988.²⁶¹ This period ended on 30 June 1994.²⁶²

6.5.1 The first period

During the first period relating to the taxation of superannuation funds and ADFs regulated by the OSSA, their exemption of income from income tax depended on compliance by the trustees of the funds with provisions of the OSSA. To be eligible for exemption,

²⁵⁸ *ITAA* pt IX – Taxation of superannuation and related business, comprising ss 267-315, as inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989, later amended by No 105 1989, applicable to assessments for the year of income in which 1 July 1988 occurred and all subsequent years.

ITAA 97 pt 3-30 div 295 – Taxation of superannuation entities, as inserted by *Tax Laws Amendment (Simplified Superannuation) Act 2007*, No 9 2007, applicable to the 2007-2008 financial year and later years.

²⁵⁹ *ITAA* ss 278-285.

²⁶⁰ *ITAA* s 281.

²⁶¹ *ITAA* 97 pt 3-1div 115, sub-div 115-A as inserted by *New Business Tax System (Integrity and Other Measures) Act 1999*, No 169 1999, provided discount capital gains to superannuation funds. *ITAA* s 115-100 provided for a discount of 33.33% for superannuation funds compared with other eligible entities which were allowed a discount of 50%.

²⁶² *OSSA* as repealed by *Occupational Superannuation Standards Amendment Act 1993*, No 84 1993.

each year superannuation funds and ADFs had to comply with their respective definitions in the OSSA and the necessary conditions, ie the operating standards. The trustees of superannuation funds and ADFs had to supply an annual return to the ISC accompanied by the prescribed levy, supply any other information and produce any documents prescribed by the OSSA or as required by the ISC.

For the taxing provisions of the superannuation funds, s 23FC²⁶³ replaced:

1. s 23F²⁶⁴ - funds established by employers for employees;
2. s 23(ja)²⁶⁵ - self-employed funds;
3. s 23FB²⁶⁶ - superannuation funds for employees and self-employed funds.

The definition of superannuation fund was inserted in *ITAA* to coincide with the introduction of OSSA and the transfer of the regulation of superannuation funds to the ISC.²⁶⁷

²⁶³ *ITAA* s 23FC, as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987 first applicable to assessments for the year of income commencing 1 July 1986.

²⁶⁴ *ITAA* s 23F provided for exemption of income, other than certain non-arm's length income, of employer sponsored funds established for the benefit of employees and their dependants.

Repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

²⁶⁵ *ITAA* s 23(ja) provided exemption from income tax for the income of a provident benefit, superannuation or retirement fund established for the benefit of self-employed persons, where the number of members of the fund was not less than 20 at any time and the rules of the fund were approved by the Commissioner of Taxation as meeting published guidelines. Repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

²⁶⁶ *ITAA* s 23FB provided for the exemption of income, other than certain non-arm's length income, of other funds that met certain rules (including a prohibition, generally, on the payment of benefits before age 55).

Repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

²⁶⁷ *ITAA* s 6(1), as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987, effective 18 December 1987. The definition of superannuation fund includes:

(a) a superannuation fund within the meaning of the *Occupational Superannuation Standards Act 1987*; and

(b) a fund to which section 23FC applies in relation to the year of income concerned.

See Chapter 2 [2.2].

For the taxing provisions of ADFs, s 23FD²⁶⁸ replaced s 23FA²⁶⁹. This also coincided with the introduction of OSSA and the transfer of the regulation of ADFs to the ISC.

Where the Insurance and Superannuation Commissioner gave a Standard Act Notice under the OSSA to the trustee of:

1. a superannuation fund,²⁷⁰ s 23FC provided exemption of income (except for certain dividends and other non-arm's length income²⁷¹) of that superannuation fund from income tax;²⁷² and
2. an ADF,²⁷³ s 23FD provided exemption of income (except for certain dividends and excessive non-arm's length income²⁷⁴) of that ADF from income tax²⁷⁵.

The taxing and regulating provisions of *ITAA* ss 23(jaa)²⁷⁶ and 23(jb)²⁷⁷ remained in the *ITAA*.

²⁶⁸ *ITAA* s 23FD substituted for *ITAA* s 23FA, as inserted by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987 first applicable to assessments for the year of income commencing 1 July 1986.

²⁶⁹ Under s 23FA, approved deposit funds that met certain requirements were exempt from tax on their investment income. The requirements related mainly to the need for the relevant fund to be established by an approved trustee to receive on deposit amounts of eligible termination payments, to deal with those amount in accordance with specified rules and to repay the amounts with accumulated earnings at the request of the depositor. Repealed by *Taxation Laws Amendment Act (No 4) 1987*, No 138 1987.

²⁷⁰ *OSSA* s 12 – notices as to satisfaction of the superannuation fund conditions.

²⁷¹ *ITAA* ss 23FC(2)-(5). *ITAA* s 23FC(6) allowed the Commissioner of Taxation to determine the extent of non-arm's length income of superannuation funds derived through any interposed partnership or trust. Because the non-arm's length income assessment provisions did not apply to s 23(ja), ss (2)-(5) only applied to income of such funds received after the date of the introduction of the *OSSA*. Chapter 3 [3.1.4.2] discusses the application of these exceptions.

²⁷² *ITAA* ss 23FC(1).

²⁷³ *OSSA* s 14 – notices as to satisfaction of the approved deposit conditions of the *OSSA*.

²⁷⁴ *ITAA* ss 23FD(2)-(5). *ITAA* s 23FD(6) allowed the Commissioner of Taxation to determine the extent of non-arm's length income of superannuation funds derived through any interposed partnership or trust.

²⁷⁵ *ITAA* s 23FD(1).

²⁷⁶ Statutory and semi-governmental superannuation funds.

²⁷⁷ Foreign superannuation funds.

6.5.2 *The second period*

From 1 July 1988, superannuation funds, ADFs and PSTs²⁷⁸ were subject to tax.²⁷⁹ The same conditions and notification for eligibility for tax concessions applied to superannuation funds and ADFs that applied prior to 1 July 1988.

A complying superannuation fund²⁸⁰, a complying ADF²⁸¹ and a PST²⁸² that fully satisfied the conditions in the OSSA for any year were eligible to be taxed at a concessional rate.²⁸³

Chapter 3 deals with the taxation of the superannuation funds, ADFs and PSTs in these periods.

The concessional tax treatment of these funds continued to encourage people to save for their own retirement.

6.6 *OSSA and OSSR*

On 23 October 1987, the Occupational Superannuation Standards Bill²⁸⁴ and other related legislation²⁸⁵ were passed by Parliament. This Bill was designed to provide a legislative framework for the operating standards and other relevant conditions with which superannuation funds and ADFs had to comply in order to be eligible to receive taxation concessions available under the *ITAA*.

²⁷⁸ *OSSA* s 15B – notices as to satisfaction of the PST conditions.
PSTs were investment vehicles for superannuation funds and ADFs, introduced with the imposition of tax on these funds. *ITAA* s 267(1) (definition of ‘PST’, as inserted by *Taxation Laws Amendment Act (No 2) 1989*, No 97 1989).

²⁷⁹ *ITAA* pt IX: div 3 for Complying Superannuation Funds; div 5 for Complying Approved Deposit Funds; div 7 for Pooled Superannuation Trusts.

²⁸⁰ *ITAA* s 267(1) (definition of ‘complying superannuation fund’).

²⁸¹ *Ibid* (definition of ‘complying approved deposit fund’).

²⁸² *Ibid* (definition of ‘pooled superannuation trusts’).

²⁸³ See above n 279.

²⁸⁴ *Occupational Superannuation Standards Bill 1987*, No 97 1987.

²⁸⁵ See above n 251.

The enactment of the *OSSA* formalised the Federal Government's commitment to its policy for providing for retirement income. The essential issue of the *OSSA* was that the sole purpose of a superannuation fund and an approved deposit fund was the establishment and maintenance for retirement and approved purposes. This sole purpose was included in the definitions of superannuation fund and approved deposit fund. This requirement existed as a prerequisite for tax concessions in different forms prior to the *OSSA*.²⁸⁶ It restricted the types of benefits that might be paid, the circumstances in which they might be provided and the activities of the fund. The *OSSA* included the regulations for compliance by superannuation funds²⁸⁷ and by approved deposit funds.²⁸⁸ These regulations were included as operational standards in the *OSSR*.²⁸⁹ They dictated the mechanism for compliance with the requirements of the *OSSA* and the *ITAA*.

Pivotal to legislative framework provided by the *OSSA* for the regulation of superannuation funds and ADFs were the definitions for the interpretation of this Act and the associated regulations.²⁹⁰ The definitions of superannuation fund and ADF provided two essential concepts that were the basis to ensure the implementation of the Federal Government's policy for retirement income. These were:

1. the sole purpose for establishing and maintaining a superannuation fund and an ADF; and
2. the indefinitely continuing nature of a superannuation fund and an ADF.

OSSA initially defined a superannuation fund to mean:

²⁸⁶ Former provisions of the *ITAA* required that a fund be 'maintained solely' for providing superannuation benefits to members. See *ITAA* ss 23F, 23FA, 23FB.

²⁸⁷ *OSSA* ss 5(2), 7(1).

²⁸⁸ *OSSA* ss 6, 8.

²⁸⁹ *OSSA* pt II referred to the *OSSR* for the prescribed operating standards.

²⁹⁰ *OSSA* s 3(1).

a fund that:

- (a) is an indefinitely continuing fund; and
 - (b) is maintained solely for either or both of the following purposes:
 - (i) the provision of benefits for each member of the fund in the event of the retirement of the member from any business, trade, profession, vocation, calling, occupation or employment in which the member is engaged;
 - (ii) the provision of benefits for dependants of each member of the fund in the event of the death of the member;
- or for either or both of those purposes and for such ancillary purposes as the Commissioner approves;²⁹¹

An ADF was defined to mean:

A fund that:

- (a) is an indefinitely continuing fund;
- (b) is maintained by an approved trustee or approved trustees solely for approved purposes; and
- (c) has approved rules;²⁹²

Approved purposes were:

- (a) receiving on deposit amounts that will be deemed by section 27D of the Tax Act to have been expended out of eligible termination payments with the meaning of that section;
- (b) dealing with such amounts, in accordance with the rules of the fund, in any way calculated directly or indirectly to enhance the value of, or render profitable, property of the fund; and
- (c) subject to any contrary requirement in the standards from time to time applicable to the fund under section 8, repaying to depositors, or the legal personal representatives of depositors, upon request, amounts deposited with the fund together with accumulated earnings on such amounts;²⁹³

By including the sole purpose as a requirement when establishing and maintaining superannuation funds and ADFs to be eligible for concessional tax treatment, the Federal Government confirmed its

²⁹¹ OSSA s 3(1). See Chapter 2 for the development of ‘superannuation fund’ and its use in the *ITAA*.

²⁹² *Ibid.*

²⁹³ *Ibid.*

intention to ensure contributions made to superannuation funds and ADFs were for providing income for retirement and old age. It also ensured that the tax concessions provided for saving for retirement were not abused by using these funds for other purposes.

These definitions included a requirement that a superannuation fund or an ADF had to be an ‘indefinitely continuing fund’ if it was to be eligible for concessional tax treatment. This requirement meant that a superannuation fund or an ADF must not be one that was to be terminated or to be wound up after a specified period.²⁹⁴ This provided protection for members’ benefits by ensuring that a fund was not required by law to be terminated or wound up after a specified time. Under the OSSA, such a requirement did not breach the rule against perpetuities.²⁹⁵ In contrast, a fund prior to the introduction of the OSSA was required by the law relating to trusts in State and Territory legislation to be vested within a specified time.²⁹⁶

In isolation, the requirement for the indefinite continuity of a superannuation fund and an ADF provided little protection for members’ benefits because there were no restrictions on the winding up of a fund provided in the OSSA or OSSR. However, coupled with the sole purpose requirement of funds, the operating standards and the imposition of a non-concessional rate of tax if these standards were not met²⁹⁷, the requirement for a fund to be

²⁹⁴ R P Meagher QC and W M Gummow, *Jacobs Law of Trusts in Australia*, (Butterworths 5th ed, 1986) [930]-[938].

²⁹⁵ OSSA s 3(2); ISC Information Circular No 18, October 1990.

²⁹⁶ This is known as the rule against perpetuities. This Rule is to prevent the vesting of an interest in property being postponed indefinitely – the vesting cannot be postponed beyond the perpetuity period. A future interest under a trust that may not vest within the perpetuity period is void.

B Marks, *Trusts & Estates*, (Taxation Institute of Australia, 2nd ed, 2009) 4-30.

²⁹⁷ For 1986-87, ITAA div 9B ss 121CC, CD for superannuation funds; ss 121DAA, DAAA for ADFs. Post-1988, ITAA pt IX: div 3 for complying superannuation funds; div 4 for non-complying funds; div 5 for complying ADFs; div 6 for non-complying ADFs.

an indefinitely continuing fund provided some protection for accrued benefits for the members' retirement.

6.7 Protection of members' benefits

Other than where relevant to the discussion, only those operating standards in the *OSSA* and the *OSSR* that apply to the protection of members' benefits in superannuation funds will be addressed in this section of the Chapter. It is considered that members' benefits were exposed to most risk in superannuation funds. The prudential supervision that applied to ADFs²⁹⁸ and PSTs²⁹⁹ in applicable legislation³⁰⁰ coupled with the *OSSA* and *OSSR* provided protection for members by requiring an 'approved trustee' and 'approved purposes' for ADFs³⁰¹ and the structural³⁰² requirements for PSTs.

The operating standards in *OSSA* and *OSSR* that provided the statutory requirements to secure members' benefits included the vesting of benefits for members arising from both employee and employer contributions,³⁰³ preservation requirements³⁰⁴ of these vested benefits and the introduction of measures to ensure greater member involvement in the control of superannuation funds.³⁰⁵ The need for protection of members' benefits was identified as the rationale for the introduction of this legislation.³⁰⁶

In addition to the compliance of the sole purpose requirement in the definition of superannuation funds, the *OSSR* detailed the

²⁹⁸ *OSSA* s 3, *OSSR* reg 19.

²⁹⁹ *OSSA* s 3A, *OSSR* reg 23.

³⁰⁰ *Companies Act 1981* replaced by *Corporations Act 1990*, *ITAA*, *Banking Act 1959*, *Life Insurance Act 1945*.

³⁰¹ *ITAA* s 27A(1) (definition of 'approved trustee', 'approved purposes').

³⁰² *ITAA* ss 102H, 267(1) (definition of 'pooled superannuation trust').

³⁰³ *OSSR* regs 6-8.

³⁰⁴ *OSSR* regs 9-11.

³⁰⁵ *OSSR* regs 13-15.

³⁰⁶ See above n 35.

requirements for the operations of superannuation funds in the operating standards relating to the protection of members' entitlements. These standards were amended during the period that the O SSA and OSSR regulated superannuation funds. One of the significant amendments was the inclusion of public sector funds for regulation by the O SSA and OSSR from 1 July 1990.³⁰⁷

These operating standards for the protection of members' benefits relating to superannuation funds included requirements that were identified as necessary to enhance the provisions for the protection for members' benefits.

The protection of members' benefits for retirement required operating standards to:

1. establish and preserve members' benefits by:
 - vesting benefits;³⁰⁸
 - restricting vesting;³⁰⁹
 - preserving benefits;³¹⁰
 - allowing portability of preserved benefits;³¹¹
 - restricting the payment of members' benefits;³¹²
 - restricting the application of benefits forgone;³¹³
 - restricting liens on benefits;³¹⁴
2. secure members' benefits by:
 - restricting:
 - lending or providing financial assistance to members or related parties;
 - borrowing;

³⁰⁷ Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 150, 25 June 1990.

³⁰⁸ O SSA s 7(2)(b); OSSR regs 6-8.

³⁰⁹ OSSR regs 8A, 18T-18Y.

³¹⁰ O SSA s 7(2)(c); OSSR regs 9-12, 21.

³¹¹ O SSA s 7(2)(e); OSSR regs 11-12, 21.

³¹² OSSR regs 11, 5AC.

³¹³ OSSR reg 17A.

³¹⁴ OSSR reg 5.

- investment in employer or related parties ie in-house assets and transactions not at arm's length;
 - the acquisition of assets from members;³¹⁵
3. formalise decision making of superannuation funds by regulating the composition of the board of trustees or board of management of a fund, or the board of a corporate trustee;³¹⁶
 4. review and regulate records by:
 - auditing the records and the financial statements;³¹⁷
 - using actuarial investigations to assess fund requirements;³¹⁸
 - limiting the reduction of accrued benefits;³¹⁹
 - regulating the provisions of the trust deed governing the fund;³²⁰
 5. report and disclose information by:
 - reporting to the ISC;
 - reporting and disclosing financial information to members;³²¹
 - lodging a prospectus where appropriate³²².

6.7.1 Establish and preserve members' benefits

The vesting and preservation provisions introduced for members' benefits in the O SSA³²³ were essential requirements underpinning the Federal Government's policy of providing retirement income. Vesting and preservation allowed members to identify their benefits and secure ownership of them. Portability allowed members to

³¹⁵ O SSR regs 16, 16A, 16B, 18BA, 18BB.

³¹⁶ O SSR regs 13-15.

³¹⁷ O SSR reg 17(1)(c).

³¹⁸ O SSR regs 17(1)(a), (b).

³¹⁹ O SSR reg 17.

³²⁰ O SSR regs 5AB, 18.

³²¹ O SSR regs 18C-P.

³²² O SSR regs 5AAA-5AAD.

³²³ O SSA ss 7(2)(b), (c).

change employment without losing their benefits.³²⁴ The operating standards in OSSR provided the requirements that applied to vesting, preservation and portability of the members' benefits and the mechanism to protect these benefits.³²⁵ The vesting, preservation and portability of members' benefits in OSSA and OSSR applied to public sector funds from 1 July 1990.³²⁶

6.7.1.1 Vesting

To vest was defined as:

[to] confer formally on [a person] an immediate fixed right of present or future possession of [authority, powers, property etc], ... possession of which is determinately fixed in a person & is subject to no contingency;³²⁷

For a superannuation fund, vesting provided a member/employee with the legal right to the entitlement accrued to that member/employee within a superannuation fund up to the date of withdrawal from the service of the employer.³²⁸

For contributions made by members or employers to a public sector fund, any reference to dates for the application of prescribed standards for private sector funds, also applied to public sector funds from 1 July 1990.³²⁹

Different vesting regulations applied to member-financed contributions and employer contributions. Prescribed vesting standards applied to amounts contributed to superannuation funds in existence before 1 July 1986 and to benefits for members

³²⁴ OSSA s 7(2)(e).

³²⁵ OSSR regs 6-11.

³²⁶ OSSR regs 6, 7, 8(2), 8, 9(1)(c), 10(2), as amended by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 150, 25 June 1990. ISC Circular No 17 [20]-[23].

³²⁷ H W Fowler and F G Fowler (eds), *The Concise Oxford Dictionary of Current English* (The Clarendon Press, 5th ed, 1964) 1448.

³²⁸ Task Force 13 [3.2].

³²⁹ See above n 307.

of funds on or after 11 June 1986. These operating standards included vesting of:

1. in respect of funds in operation on 30 June 1986, benefits arising from contributions made prior to 1 July 1987, by or on behalf of a member (other than employers' voluntary contributions), but not earnings made prior to 1 July 1987 on such contributions;³³⁰
2. in respect of all funds, benefits arising from contributions made on or after 1 July 1986 by or on behalf of a member (other than employers' voluntary contributions), including earnings on such contributions;³³¹
3. in respect of all funds, benefits arising from contributions made by an employer in relation to a member in accordance with a prescribed agreement or award.³³² A 'prescribed agreement or award' was defined as meaning 'an agreement or award (including a consent award) that is certified or made by a Commonwealth industrial authority or State industrial authority on or after 1 July 1986'.³³³

A member's 'contributions' to a superannuation fund included any amount transferred to that superannuation fund that was vested in the member in a prior superannuation fund or an ADF.³³⁴

Member-financed benefits were defined in terms of the amount calculated on withdrawal of benefits from the superannuation fund.³³⁵ They were the member's contribution with net earnings³³⁶

³³⁰ *OSSR* reg 6.

³³¹ *OSSR* reg 7.

³³² *OSSR* reg 8. The manner of determining the vested benefit in particular circumstances are in ISC Circular No 8 [31]-[42].

³³³ *OSSR* reg 3.

³³⁴ *OSSR* reg 3(2).

³³⁵ *Ibid.*

³³⁶ *OSSR* reg 3(3). 'Net earnings' of a superannuation fund were to be read as a reference: to the amount of the earnings of the fund after deducting the amount of such administrative and other costs as are attributable to the amount of contributions received by the fund and

allotted to the member based on the contributions.³³⁷ Where the benefits were purchased under a life insurance policy, they were the amount purchased by the member's contribution, whether the benefits arose on death, retirement, disablement or some other event.³³⁸ Where withdrawal benefits were determined on the basis of the member's salary (or the salary averaged over some period), the member-financed benefits were determined by reference to the member's contribution rate, length of membership and salary (or appropriate average salary) at the time of withdrawal.³³⁹

Contributions made by a member to a superannuation fund and transferred to another superannuation fund or an approved deposit fund were member-financed benefits.³⁴⁰

The operating standards regulating the vesting of members' benefits evolved to define the terms and the application of those terms that related to vesting. This evolution ensured the members' benefits were clearly defined and able to be quantified.³⁴¹ Circulars published by the Commissioner of the ISC provided interpretation of the regulations relating to vesting of members' benefits.³⁴²

The operating standards that applied to vesting of members' benefits provided certainty of a member's entitlement to benefits. This certainty encouraged persons to save and allowed them to plan for retirement. It provided some protection of a member's rights by prescribing a method for calculating benefits.

after allowing for any averaging of the earnings of the fund, in accordance with the trust deed, to take into account possible or actual periodic fluctuations in those earnings.

337 *OSSR* reg 3(1)[a] (definition of 'member-financed benefits').

338 *Ibid* [(b)].

339 *Ibid* [(c)]; *OSSR* reg 3(5).

340 *OSSR* reg 3(2).

341 *OSSR* regs 3, 3B, 6-9.

342 Circulars No 2 [3]-[4], 3[4]-[9], 5[10]-[14], 8[17]-[30], 17 [20]-[21], 20 [3]-[6].

6.7.1.2 Restricting vesting

From 1 July 1992, a superannuation fund that was not a defined benefit fund and guaranteed by the Commonwealth, a State or a Territory had to comply with a minimum funding standard in the form of a limitation on the rate of increase of the member's vested benefits that arose directly or indirectly from amounts contributed to the fund.³⁴³ The trustee was prohibited from increasing the vested benefits of a member such that if the fund was immediately terminated after the vesting of those benefits, there would be insufficient assets in the fund to pay the 'minimum requisite benefit'³⁴⁴ in respect of all other members of the fund.³⁴⁵ This did not prohibit a higher rate of return being provided by the trustee if there were sufficient reserves available to be used to smooth the shortfall in the rate set during the year of income.³⁴⁶ It did not prevent a negative or zero rate of return being set.³⁴⁷

Also from 1 July 1992, the trustees of a defined benefit superannuation fund were required to obtain a certificate of contribution and solvency for the fund from an actuary.³⁴⁸ This requirement is dealt with in detail in paragraph 6.7.4 of this Chapter below.

³⁴³ OSSR reg 8A(1), (2). OSSR reg 8A was inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1992 No 223, 30 June 1992.

³⁴⁴ OSSR reg 3(1), as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)* Statutory Rules 1992 No 223, 30 June 1992. 'Minimum requisite benefit, in relation to a member of a superannuation fund, means the minimum benefit required to be vested in the member by the superannuation fund conditions.'

³⁴⁵ OSSR reg 8A(3).

³⁴⁶ ISC Circular No 33 [49]-[52].

³⁴⁷ Ibid.

³⁴⁸ OSSR regs 18T-18X, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1992 No 223, 30 June 1992. The regulations introduced by this amendment were to coincide with the commencement of the *Superannuation Guarantee (Administration) Act 1992*. The Government decided to delay the application of the rules ([18T]-18[Y]) for Contribution and Solvency Certificates until 1 July 1994. ISC Circular No 33 [70].

Employer contributions in a defined benefit fund were required to be made in accordance with the last actuarial investigation.³⁴⁹ The trustee of a superannuation fund was required to give a copy of the certificate of contribution and solvency to the employer who contributed to the superannuation fund for a member of that fund.³⁵⁰

The trustee was prohibited from vesting any further benefits in the fund members, if an employer failed to make contributions to a superannuation fund in a year of income in accordance with the rate or rates specified in the certificate of contribution and solvency. This restriction applied until the employer, within 12 months of the end of the year of income, paid either:

- the required contribution amount as specified in the relevant certificate; or
- the required contribution amount as specified in another certificate.³⁵¹

The vesting requirements of the *OSSA* and *OSSR* provided a mechanism for members to identify and quantify their entitlement to benefits within a superannuation fund. This supported the Federal Government's intention of providing income for members in their retirement.

6.7.1.3 *Preservation*

Preserve is defined as: 'undisturbed for private use'.³⁵²

³⁴⁹ *OSSR* reg 18Y. This regulation was replaced by a similar but more defined regulation by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1993 No 213, 27 July 1993.

³⁵⁰ *OSSR* regs 18U(5), 18V(3), 18W.

³⁵¹ *OSSR* reg 18X.

³⁵² Oxford Dictionary n 327 964.

To protect benefits until retirement, except in certain circumstances, the OSSR required certain vested benefits to be preserved until a member's retirement from the workforce at or after the age of 55:

1. benefits arising from contributions made by an employer in relation to a member in accordance with a prescribed agreement or award on or after 1 July 1986;³⁵³
2. the amount of any other new or improved employer financed benefits vested in a member and arising from any arrangement or agreement made on or after 22 December 1986;³⁵⁴
3. any amounts transferred to the fund from another fund consequent upon the withdrawal of the member from the latter fund.

Benefits could be paid if the member retired from the workforce and attained the age of not less than 55 years.³⁵⁵

These benefits could be paid before age 55 years if the member:

1. retired from the workforce because of permanent incapacity or permanent disability (certified by two medical practitioners);³⁵⁶
2. died;³⁵⁷ or
3. permanently departed from Australia.³⁵⁸

Benefits totalling less than \$500 were not required to be preserved.³⁵⁹

³⁵³ OSSR reg 9.

³⁵⁴ OSSR reg 10.

³⁵⁵ OSSR reg 11(a)(ii).

³⁵⁶ OSSR reg 11(a)(iii)(A), reg 11(b).

³⁵⁷ OSSR reg 11(a)(iii)(B).

³⁵⁸ OSSR reg 11(a)(iii)(C).

³⁵⁹ OSSR reg 12.

The application of the prescribed operating standards for preservation of members' benefits was expanded in a Circular issued by the ISC Commissioner.³⁶⁰ It addressed a number of issues indicating how the Commissioner of the ISC would interpret them.

The preservation requirements of the *OSSA* and *OSSR* for members' benefits assisted in the implementation of the Federal Governments' policy of providing income for people's retirement. Preservation assisted the notion that members' benefits would be available when required. This encouraged members to save for retirement and to have confidence in the superannuation system.

6.7.1.4 *Portability*

Where a member had not retired and attained the age 55 years or was not entitled to another of the prescribed circumstances for payment of benefits, the benefits had to be preserved:

1. in the fund to which the contributions were paid;³⁶¹ or
2. transferred directly to:
 - (i) another superannuation fund;
 - (ii) an ADF;
 - (iii) a deferred annuity until the member retired from the workforce aged 55 years or complied with the exceptional circumstances.³⁶²

By providing the mechanism in the *OSSA* and the *OSSR* for the transfer of members' benefits, the Federal Government confirmed their policy intent to provide income for retirement and ensure that members' benefits were available when required.

³⁶⁰ ISC Circular No 8 October 1988 [31]-[66].

³⁶¹ *OSSR* reg 11(c)(i).

³⁶² *OSSR* reg 11(c)(ii).

6.7.1.5 Time for paying benefits

The restrictions of the circumstances in which the trustee of a superannuation fund could pay benefits to members complemented the requirement for the sole purpose of the funds to be for retirement of the members and their dependants in the event of their death.³⁶³ The restrictive approved purposes and payment of benefits that applied to ADFs also complemented the sole purpose requirement of superannuation funds.³⁶⁴

The restrictions applied to payments made by the trustee of a superannuation fund other than those specifically for retirement. These payments had to be made for ‘ancillary purposes’.³⁶⁵

Prior to 1 July 1990, benefits had to be payable only on the member’s retirement from a business, trade, profession, vocation, calling, occupation or employment in which the member had been engaged.³⁶⁶ Subsequently in *OSSA*, the definition of superannuation fund was amended to read that a superannuation fund was maintained solely for one or more of the following purposes and the payment of benefits could be made to a member on reaching a prescribed age although the member had not retired³⁶⁷:

- (i) ...
- (ii) the provision of benefits for each member of the fund in the event of the member attaining a particular age (being an age not less than the age prescribed by the regulations) without having retired from

³⁶³ *OSSA* s 7(2)(d); *OSSR* regs 6-10.

³⁶⁴ *OSSA* s 8(2)(c); *OSSR* reg 21.

³⁶⁵ The benefits as ancillary purposes were set out in ISC Circular No 8 [8]-[10], October 1988 applied for period 1 July 1986 to 30 June 1988. From 1 July 1988, the provisions included in the trust deed governing a fund accepted by ISC - ISC Circular No 8 [11]. Circular No 10, July 1989 added further advice relating to approved ancillary purposes.

³⁶⁶ *OSSA* s 3(1).

³⁶⁷ Regulation 5AC – standards: ages for payment of benefits in the *OSSR*, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 185, 26 June 1990.

- any business, trade, profession, vocation, calling, occupation or employment in which the member is engaged;
- (iii) the provision of benefits for dependants of each member of the fund in the event of the death of the member, being a death occurring before:
- (A) the member's retirement from any business, trade, profession, vocation, calling, occupation or employment in which the member is engaged;
 - (B) the member attains a particular age (being an age not less than the age prescribed for the purposes of subparagraph (ii)) without having retired from any business, trade, profession, vocation, calling, occupation or employment in which the member is engaged;
- whichever is earlier;
- or for one or more of those purposes and for such ancillary purposes as the Commissioner approves in writing.³⁶⁸

This reflected a more flexible approach to retirement, which aimed to assure continued reinforcement of underlying policy to encourage persons to save for their retirement and associated purposes.

From 22 December 1992, the definition of superannuation fund was further amended to allow more flexibility by permitting retired people to transfer their pensions from one provider to another.

...

- (iv) the provision of pensions for each transferred retiree member of the fund;³⁶⁹

The restrictions that the OSSR applied to the payment of members' benefits prohibited their being made available to members prior to

³⁶⁸ OSSA s 3(1) (definition of 'superannuation fund' definition (b)(ii), as repealed by *Occupation Superannuation (Reasonable Benefit Limits) Amendment Bill 1990*, No 61 1990; (b)(ii)-(iii); as inserted *Occupation Superannuation (Reasonable Benefit Limits) Amendment Bill 1990*, No 61 1990, effective 1 July 1990).

³⁶⁹ OSSA s 3(1) (definition of 'superannuation fund' '... (iv) as inserted by *Taxation Laws Amendment (Superannuation) Act 1992*, No 208 1992).

retirement or for ancillary purposes. This was in line with the Federal Government's retirement policy.

6.7.1.6 *The application of benefits forgone*

From 1 July 1990, in the case of an allocated fund, any benefits to which a member had ceased to have rights were to be applied for one or other of the approved purposes, either within the year of income in which the right to receive benefits ceased, or within six months after the year of income.³⁷⁰ Approved purposes to be applied were:

- the provision of benefits that other members or their dependants had rights to receive from the fund;³⁷¹
- the provision for other members or their dependants of additional benefits, on a basis that the ISC was satisfied was reasonable;³⁷² or
- any other purpose approved in writing by the ISC³⁷³.

In the case of an unallocated fund, any additional benefits that resulted from the cessation of the right of a member to receive benefits had to be applied on a basis that the ISC was satisfied was reasonable.³⁷⁴ If the money remained within the unallocated amount in the superannuation fund, the effect was that the contributions payable by the employer to provide specified benefits were reduced.

This prescribed application of the benefits forgone by members ensured that the benefits were applied for purposes that the

³⁷⁰ OSSR reg 17A, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 185, 2 July 1990. ISC Circular 18 [65]-[67].

Prior to OSSR reg 17A, the requirements relating to the application of benefits of members whose rights to them had ceased were in ITAA s 23F.

³⁷¹ OSSR reg 17A(a)(i).

³⁷² OSSR reg 17A(a)(ii).

³⁷³ OSSR reg 17A(a)(iii). ISC Circular No 18 [65] referred to Public Information Bulletin No 6 for 'purposes approved'.

³⁷⁴ OSSR reg 17A(b). This was similar to requirement of ITAA s 23F.

Federal Government intended within the superannuation environment.

6.7.1.7 *Limiting the reduction of accrued benefits*

Prior to 21 August 1990, a member's accrued benefit could only be reduced if all members or the ISC approved in writing.³⁷⁵

After 21 August 1990, the OSSR was amended to prohibit a member's accrued benefits being reduced retrospectively except in certain circumstances permitted by the regulation.³⁷⁶ These circumstances for reduction were where:

- the reduction was required because of, and did not exceed the value of, any tax payable on fund income; or
- the reduction was required to enable the fund to comply with the prescribed standards; or
- the members approved in writing of the reduction; or
- the ISC approved the reduction in writing.³⁷⁷

6.7.1.8 *Liens on benefits*

Neither the OSSA nor OSSR defined the term 'lien'. Lien is defined in the Oxford Dictionary as a right to keep possession of property till debt due in respect of it is discharged.³⁷⁸

Under the original OSSR, an employer or any other person who contributed to the superannuation was precluded from placing liens in favour of a contributor to a fund in respect of benefits required by the OSSR to be vested or preserved.³⁷⁹ This ensured that the rights of members for benefits on retirement by the vesting

³⁷⁵ OSSR reg 17(1)(d); ISC Circular No 5 [40], No 8 [82]-[86].

³⁷⁶ Commonwealth Government of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules No 275, 21 August 1990.

³⁷⁷ Substituted OSSR reg 17(1)(d).

³⁷⁸ Oxford Dictionary, n 328 700.

³⁷⁹ OSSR reg 5.

and preservation requirements were not defeated through the exercise of liens over those benefits.

This right to record a lien on a member's benefits arose from the governing trust documents. A debt by a member to an employer might have arisen as a result of a loan by the employer to the employee. Losses might have arisen as a result of the employee's theft or misuse of, or damages caused by the employee to, the employer's property or a failure by a former employee to observe a restrictive covenant.

Under the *OSSR*, a lien could be exercised over an amount arising from employer contributions made to a superannuation funds under an arrangement entered into prior 22 December 1986. Also a person who was not the employer or other contributor to the superannuation fund eg a financier, could have placed a lien over the member's benefits, regardless of whether the benefits were vested or preserved under the *OSSR*.

Subsequent to an amendment to the *OSSR*³⁸⁰, commencing on 21 August 1990, a trustee could not be a party, or give effect, to 'the exercise of a lien by another person over prescribed benefits'. The definition of exercising a lien by another included a reference to:

- (a) the making by a member of the fund of an arrangement in writing that provides for the lien to be exercised in respect of an identified debt owed by the member to the person; and
- (b) the giving of notice of the intention of the person to exercise the lien in respect of an identified debt owed by a member to the person if exercise of the lien is required to protect the interests of that person; and

³⁸⁰ Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 275, 21 August 1990.

- (c) the taking by the person of any action required for the purpose giving effect to the lien in respect of an identified debt owed by a member to the person.³⁸¹

The amended regulation included the definition of ‘prescribed benefits’ to mean benefits that were required by *OSSR* to be vested in the member and preserved by the fund.³⁸² The amended regulation provided an exception in that the trustee in its capacity as trustee could exercise a lien over the benefits vested or preserved under the *OSSR*, if the member owed money to the trustee - a potential problem if the employer was also the trustee.³⁸³

Where a person exercised a lien over prescribed benefits before the amendment of the *OSSR*, no action could be taken to vary that lien except to limit its scope or remove it. Liens that were exercised:

1. before the introduction of the original Regulation 5 on 22 December 1987; or
2. in accordance with that original regulation between 22 December 1987 and the amendment on 21 August 1990, continued to be governed by the original regulation.³⁸⁴

The prohibition of exercising liens over vested or preserved benefits was a further mechanism implemented by the Federal Government to protect members’ benefits and ensure that the entitlements would be available for members on retirement.

The identification of the individual member’s benefits and acknowledgment of the member’s ownership provided by the vesting and preservation were essential steps to protecting members’ benefits.

³⁸¹ *OSSR* reg 5(6).

³⁸² *OSSR* reg 5(5).

³⁸³ *OSSR* reg 5(3).

³⁸⁴ ISC Circular No 3 [11], No 5 [9], No 20 [11]-[13].

The portability of and restrictions on payment and use of these benefits were consistent with the Federal Government's policy to provide income for members on their retirement.

6.7.2 Security of members' benefits

Despite the identification of their benefits as a basic means for the protection of members' benefits, there was still a threat to them. Members' benefits were vulnerable because of the investments by trustees, especially in related entities as loans or equity. The Committees considered these to be inappropriate and precarious.³⁸⁵ OSSA and OSSR addressed this problem.

Operating standards were introduced to provide restriction on investments of superannuation funds made by trustees. These standards complemented the sole purpose for establishing and maintaining superannuation funds.

OSSR³⁸⁶ prescribed operating standards relating to three aspects of a superannuation fund's investments:

1. loans to members, either directly or indirectly, were prohibited with limited exceptions.³⁸⁷ Where the provisions of the governing rules for a private sector fund established before 16 December 1985, or a public sector fund established before 25 May 1988 allowed these loans, an exception applied;³⁸⁸
2. trustees of superannuation funds were prohibited from borrowing, except to secure temporary finance;³⁸⁹

³⁸⁵ The Asprey Report [21.101]; the Hancock Report 104-5 [7.13]-[7.17]; the Campbell Report 349 [20.126]; the Task Force Report 37-8 [4.32]-[4.39].

³⁸⁶ OSSR reg 16.

³⁸⁷ OSSR reg 16(1)(a).

³⁸⁸ OSSR reg 16(2).

³⁸⁹ OSSR reg 16(1)(b).

3. all investments of the superannuation fund, except those permitted by the in-house asset rules, had to be made on an arm's length basis³⁹⁰.

6.7.2.1 *Restricted lending*

The trustee of a superannuation fund was prohibited from lending the fund's money to any superannuation fund members.³⁹¹

Exceptions applied where under the governing rules in force on 16 December 1985 for a private sector fund or 25 May 1988 for a public sector fund³⁹², the trustees were empowered to grant loans to members or had lent money to members and that lending to members was not expressly prohibited, the trustee could continue to lend money to members. The power of the trustee to lend money in the governing rules was prohibited from being varied except to limit that power or to remove it.³⁹³ Where the governing rules did not expressly allow the trustees to lend to members but also did not prohibit it, the ISC looked at past practices of the trustees in lending to members in determining whether this standard had been complied with.³⁹⁴

6.7.2.2 *Restricted borrowing*

The trustee was prohibited from borrowing, whether by way of a secured or unsecured loan, other than to secure temporary finance.³⁹⁵ Initially OSSR stipulated that the temporary finance should be by way of overdraft with an eligible bank³⁹⁶. This

³⁹⁰ OSSR reg 16(1)(c).

³⁹¹ OSSR regs 16(1)(a), (2), (15).

³⁹² ISC Circular No 17 [33].

³⁹³ OSSR reg 16(2)(f).

³⁹⁴ ISC Circular No 17 [32].

³⁹⁵ OSSR reg 16(1)(b).

³⁹⁶ OSSR reg 3 defined 'eligible bank' as

- (a) a savings bank or trading bank as defined by subsection 5(1) of the Banking Act 1959; or
- (b) a public authority constituted by a law of a State or Territory, being a public authority that carries on banking business.

ISC Circular No 8 [73] advised that:

requirement was removed from *OSSR* and the exception was restricted to temporary finance.³⁹⁷ ‘Temporary finance’ was defined to mean finance arranged by borrowing in order to overcome cash flow problems in the payment of superannuation benefits.³⁹⁸

The Federal Court in *Tefonu Pty Ltd v ISC*³⁹⁹ considered the meaning of ‘temporary finance’. Breazley J said

Such a borrowing must have a quality of transience about it, which is to be ascertained from the purpose of the borrowing and the period of time involved in the borrowing. The purpose must be to provide finance for a passing or transitory need.

His Honour also said that although the period of borrowing must be for a short term, it is not sufficient that the finance be merely limited in time.⁴⁰⁰

If the trustees of a private sector fund had, on or before 11 June 1986, borrowed money that did not comply with the operating standards, they were required as soon as practicable to repay the amounts borrowed or ensure that the fund complied with the standard and repay the borrowed amount as soon as practicable but no later than 30 June 1995.⁴⁰¹ In the case of a public sector fund, the operating standard had to be satisfied no later than 30 June 2000.⁴⁰²

Temporary finance in this context would extend to borrowing to overcome temporary cash flow problems, such as would arise where the number of resignations greatly exceeded expectations and required a large payout of benefits. However, the term should not be interpreted to encompass borrowing for the purpose of augmenting a fund’s resources available for investment.

³⁹⁷ Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 150, 25 June 1990.

³⁹⁸ ISC Circular No 8 [73] prior to insertion of *OSSR* reg 16(5). *OSSR* reg 16(5), as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 150, 1 July 1990.

³⁹⁹ 93 ATC 4727, 4735.

⁴⁰⁰ *Ibid.*

⁴⁰¹ *OSSR* reg 16(3), (3A)(b).

⁴⁰² *OSSR* reg 16(3)(b).

6.7.2.3 Arm's Length Investments and In House Assets⁴⁰³

All investments (other than investments which would have complied with the 'in-house asset' limits prescribed by the *ITAA* s 121C) had to be made on an arm's length basis.⁴⁰⁴ Initially, the *OSSR*⁴⁰⁵ referred the application of the in-house asset rules to relevant provisions of the *ITAA*.⁴⁰⁶

From 1 July 1990, similar provisions in the *ITAA* for the application of the in-house asset rule were incorporated into the *OSSR* with reference to the *ITAA* omitted⁴⁰⁷. With the exception of imposing the in-house asset restrictions on public sector funds⁴⁰⁸ and life assurance companies⁴⁰⁹, no substantive changes were made to the new regulation.⁴¹⁰

The basic rule that applied to private sector funds established on or after 12 March 1985 and to public sector funds established on or after 1 July 1990 was that, at all times during a year of income, the cost of the in-house assets of a fund must not exceed 10% of the cost of all the assets of the fund.⁴¹¹ A transitional rule applied up to and including the 1994-1995 year of income for private sector funds in existence at 11 March 1985 effectively providing a 10 year period for these funds to satisfy the basic rule.⁴¹² A similar

⁴⁰³ *OSSR* regs 16, 16A, 16B; ISC Circular No 18 [30]-[42].

⁴⁰⁴ *OSSR* reg 16(1)(c).

⁴⁰⁵ *OSSR* reg 16(4).

⁴⁰⁶ *ITAA* ss 121C(4), (5), (6), as inserted by *Taxation Laws Amendment Act (No 2) 1985* No 123 1985 first applicable to assessments for the year of income commencing 1 July 1985. The paragraphs on In-house Asset Rules in *Income Tax Ruling* IT 2293 were superseded by [34]-[62] of the ISC Circular No 18.

⁴⁰⁷ *OSSR* reg 16A, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1990 No 185, 29 June 1990.

⁴⁰⁸ *OSSR* reg 16A(1). The definition of in-house asset does not include investment in government securities by a public sector fund.

⁴⁰⁹ *Ibid*. The definition of in-house asset does not include a life insurance policy on a member where the employer sponsor is a life assurance company.

⁴¹⁰ ISC Circular No 18 [30].

⁴¹¹ *OSSR* reg 16A(17)(a) for private sector funds; *OSSR* reg 16A(18)(a) for public sector funds.

⁴¹² *OSSR* reg 16A(17)(b).

transitional rule applied up to and including the income year ending 30 June 2000 for public sector funds established before 1 July 1990.⁴¹³ The transitional rules required that the cost of in-house assets of those funds did not exceed, at any time during the year of income, the greater of:

- the cost of the fund's in-house assets as at 11 March 1985 for private sector funds and 1 July 1990 for public sector funds; or
- 10% of the cost of all the assets of the fund.

The definition of in-house asset referred to a loan to, or an investment in, an employer sponsor, or an associate⁴¹⁴ of an employer sponsor of the superannuation fund.⁴¹⁵

The definition did not restrict an in-house asset to loans. It included investments ie assets acquired by a superannuation fund to secure profitable returns, especially interest or income.⁴¹⁶ By definition, investments included shares and debentures.

Investment in government securities by a public sector fund was excluded from the definition of in-house asset.⁴¹⁷ Investment income received during the year was taken to be an asset of the fund.⁴¹⁸ Guarantees were also included as in-house assets in certain circumstances.⁴¹⁹

The definition of an 'employer sponsor' of a superannuation for the purposes of the operating standards relating to the restrictions on in-house asset was:

⁴¹³ *OSSR* reg 16A(18)(b).

⁴¹⁴ *OSSR* regs 16A(2), (3).

ITAA s 26AAB(14) (definition of 'associate' in broad terms, any person who, by reason of business or family connections, was regarded as being associated with a particular person.)

⁴¹⁵ *OSSR* reg 16A(1).

⁴¹⁶ *The Macquarie Dictionary*, (The Macquarie Library Pty Ltd, 2nd ed, 1987) 920.

⁴¹⁷ *Ibid.*

⁴¹⁸ *OSSR* reg 16A(4).

⁴¹⁹ *OSSR* regs 16A(11), (12).

- (a) an employer of a member of the fund; or
 - (b) a company in which an employer of a member of the fund had a controlling interest; or
 - (c) if an employer of the member was a company – a person who was connected with that company
- who contributed to the fund in respect of the member or his or her dependants, where a member of a superannuation fund had, or dependants of a member had, a right to receive benefits from the fund.⁴²⁰

Persons who were ‘connected’ with a company that was the employer of a member were:

- a person who had a controlling interest in the employer;
- a person, being a company, in which a controlling interest was held by a person that also had a controlling interest in the employer; or
- a person who was a beneficial owner of shares in the employer.⁴²¹

This definition applied to any company in a group of companies consisting of a holding company and its subsidiaries or sub-subsidiaries.⁴²²

An employer continued to qualify as an employer sponsor of the superannuation fund, even though the employer made no contributions to the superannuation fund in respect of a member or dependants during a particular year of income.⁴²³

⁴²⁰ *OSSR* reg 16A(5).

⁴²¹ *OSSR* reg 16A(6).

⁴²² *Ibid* (c).

⁴²³ *Case Y10*, 91 ATC 177 – an employer which had made no contributions for a period of seven years but which was the sole contributor in four earlier years was held to be an employer sponsor under former *ITAA* s 121C(2).

The Commissioner of the ISC could treat the loan or investment as not being an in-house asset having regard to:

- the amount of the loan;
- the value of the shares; and
- any other matters that the Commissioner considered relevant.⁴²⁴

Safeguarding provisions were included in the operating standards to prevent circumvention of the in-house asset rules.⁴²⁵ The Commissioner also had the option to exercise discretion to treat an asset as not being an in-house asset in specific circumstances.⁴²⁶ The operating standards also contained provisions for determining the cost of in-house assets.⁴²⁷

From 29 January 1993, superannuation funds were prohibited from acquiring new in-house assets if:

- (a) the market value of in-house assets of the fund already exceeds 5% of the market value of all assets of the fund; or
- (b) in consequence of the investment, the market value of in-house assets of the fund would exceed 5% of the market value of all assets of the fund.⁴²⁸

By restricting the investment by trustees in the employer or related parties, the OSSA and OSSR protected employees from losing their jobs and their superannuation benefits at the same time if the employer or related party experienced financial difficulties. It ensured that the trustees acted in the interest of members and not the employer or related parties.

⁴²⁴ OSSR reg 16A(13). The Commissioner had to be satisfied that it would be reasonable, having regard to the factors in ss [44]-[46] of ISC Circular No 18. Generally loans to members were not permitted.

⁴²⁵ OSSR reg 16(8), (9).

⁴²⁶ OSSR reg 16(13).

⁴²⁷ OSSR regs 16A(4), (7), (9), (11). ISC Circular No 18 [49]-[52]; [55]-[60].

⁴²⁸ OSSR reg 16B. Inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)* Statutory Rules 1993 No 14, 22 January 1993.

6.7.2.4 *Restricted acquisition of assets from members.*

From 1 July 1993, the OSSR prohibited the trustees of a superannuation fund from intentionally acquiring an asset from a member, or a relative of a member⁴²⁹ of the fund.⁴³⁰ Exceptions included the acquisition of listed securities⁴³¹ at market value⁴³². The prohibition also did not apply to an 'excluded superannuation fund'⁴³³ that acquired 'business real property'⁴³⁴ at market value if the total value of this type of property acquired was not more than 40%. Anti-avoidance measures were included to prevent assets being acquired by trustees from persons connected with a member or relative where that acquisition had been undertaken to avoid the prohibition.⁴³⁵

This prohibition provided integrity to the investment process by trustees. It complemented the requirements in the legislation enacted by the various States and Territories of Australia to establish the duties and responsibilities of trustees and to provide fiduciary protection of assets invested for retirement.

The restrictions imposed by the OSSA and OSSR on the use by their trustees of members' benefits accumulated within the superannuation funds reduced the risk of loss of these benefits. They reduced the exposure to potential risk associated with

429 OSSR reg 18BA(3) (definition 'relative' referred to ITAA s 6(1) in relation to any person, means any of the following, namely:
 (a) the parent, grandparent, brother, sister, uncle, aunt, nephew, niece, lineal descendant or adopted child of that person or of his or her spouse; and
 (b) the spouse of that person or any other person specified in paragraph (a)).

430 OSSR reg 18BB.

431 OSSR reg 18BB(4) (definition of 'listed security' to mean a share, unit, bond or debenture, right or option or any other security listed on the Australian stock exchange),

432 *Abrahams v FC of T* (1944) 70 CLR 23, defined market value to be 'the price which a willing but not anxious vendor could reasonably expect to obtain and a hypothetical willing but not anxious purchaser could reasonably expect to have to pay ... if the vendor and purchaser had got together and agreed on a price in friendly negotiation.'

433 OSSR reg 18BB(4) (definition of 'excluded superannuation fund' to mean 'a superannuation fund of which there are fewer than 5 members').

434 OSSR reg 18BB(4) (definition of 'business real property' to mean any freehold or leasehold interest in real property used wholly and exclusively for business).

435 OSSR reg 18BB(3).

investing in or lending to the employer or lending to the members or related parties.

The combination of the requirements of sole purpose of a superannuation fund, vesting, preservation and portability of members' benefits and the restriction of use of those benefits provided some protection for benefits. The combination provided the basis for and was consistent with the Federal Government's policy to encourage people to save for their own retirement. These measures attempted to ensure that members' benefits would be available when required.

6.7.3 *Trustees and composition of board*

Superannuation funds were generally trusts.⁴³⁶ Trust deeds imposed trustee obligations on the persons responsible for decision making and the operations of the superannuation fund. The State and Territory legislation governed corporate trustees.⁴³⁷ Under the regulations of the *OSSR*, the trustee of a superannuation fund was required to give information to the Commissioner.⁴³⁸ The Commissioner also might require the trustee to produce documents.⁴³⁹ Concessional tax treatment of a superannuation fund depended on the trustee providing this information to the Commissioner⁴⁴⁰ and the Commissioner being satisfied that the superannuation fund met the required conditions in a particular year of income.⁴⁴¹ The Commissioner and the members of a superannuation fund depended on trustees to act in the best interests of the members. The trustee was required to certify that

⁴³⁶ See Chapter 2 [2.1].

⁴³⁷ *Trustee Companies Act 1963* (NSW); *Trustee Companies Act 1968-1984* (Qld); *Trustee Companies Act 1953* (Tas); *Trustee Companies Act 1987* (WA); *Companies (Trustees and Personal Representatives) Act 1981* (NT); *Trustee Companies Act 1984* (Vic); *Trustee Companies Act 1947* (ACT); *Trustee Companies Act 1988* (SA).

⁴³⁸ *OSSA* s 10.

⁴³⁹ *OSSA* s 11.

⁴⁴⁰ *OSSA* s 10(1).

⁴⁴¹ *OSSA* s 12.

the information provided was correct and that the superannuation fund satisfied the conditions applicable to the fund in relation to the year of income specified in the return.⁴⁴²

Measures for minimal supervision included greater representation on the boards of trustees⁴⁴³, a greater degree of audit⁴⁴⁴ and disclosure of information to members on the operation of the funds⁴⁴⁵. These standards provided a mechanism for protection of members' benefits by including independent involvement in decision making, review of financial information and disclosure of this information.

As part of the process of protecting members' benefits, those who made decisions about the activities of superannuation funds had to act in the members' best interests. The *OSSA* enhanced the decision making process by imposing requirements relating to the representation on a superannuation fund's management board or committee if it exercised actual control over the policies of the fund.

Funds established on or after 16 December 1985 had to have representation of members as trustees, on the management board, or the board of a corporate trustee.⁴⁴⁶ The representation requirement was dependent on the size of the fund. The concept of classifying superannuation funds according to size was introduced in relation to the control of the decision making process.

⁴⁴² *OSSR* reg 24(1), Form 1 of the Schedule.

⁴⁴³ *OSSA* s 7(2)(j); *OSSR* regs 13-15.

⁴⁴⁴ *OSSA* s 7(2)(k); *OSSR* reg 17(1)(c).

⁴⁴⁵ *OSSA* s 7(2)(m); *OSSR* reg 17.

⁴⁴⁶ *OSSR* reg 13; *ISC Circulars* No 2, 3, 5, 8, 17, 24.

6.7.3.1 'Large funds'

A superannuation fund with more than 200 members ('a large fund') had to have equal representation of employer representatives⁴⁴⁷ and member representatives⁴⁴⁸ on the body that exercised control over policies of the fund. It could be a board or committee of trustees, a management board or committee, body corporate or other management body.⁴⁴⁹

The trust deed could provide for the appointment of an independent trustee, not entitled to a casting vote, where requested by either the employer or member representatives.⁴⁵⁰

Written approval for unequal representation on its trustee or management board could be given by the Commissioner of the ISC generally, in a particular case or a particular class of cases.⁴⁵¹

Some superannuation funds offered to the public. Boards of a trustee company in these situations were not required to have equal representation. This exemption was subject to, where an employer enrolled 200 or more members into the fund, the establishment of a committee or similar arrangement with equal employer and member nominated persons being appointed. This would be responsible for a sub-plan and the day-to-day administrative operations of the sub-plan.⁴⁵²

⁴⁴⁷ OISSR reg 3(1) (definition of 'employer representative' to be 'a member ... nominated by the employer or employers of the members of the fund or by an organization nominated by that employer or those employers as representing the interests of that employer or those employers').

⁴⁴⁸ Ibid. (Definition of 'member representative' to be 'a member ... nominated by the members of the fund or by a trade union or other organization representing the interests of those members').

⁴⁴⁹ Ibid reg 13(a)-(c).

⁴⁵⁰ Ibid reg 13(d).

⁴⁵¹ Ibid reg 13(e).

⁴⁵² Occupational Superannuation Commissioner, *Interim Group Information Circular No 2* [10]-[11]; ISC Circular No 8 [68]-[71].

Vacancies had to be filled within 60 days.⁴⁵³

Employers could nominate the employer representatives directly, or nominate an employer organisation that then would nominate the representatives. Members or their trade union or other organization could nominate the members' representatives.⁴⁵⁴

From 1 July 1987 for private sector funds and from 1 July 1990 public sector funds, decisions by the trustee of large funds or board or management committee required not less than two-thirds of the vote in favour of a decision.⁴⁵⁵

6.7.3.2 'Small funds'

A 'small fund', a superannuation fund having fewer than 200 members, could conform with the standards for large superannuation funds.⁴⁵⁶

Alternatively, the trustee or trustees had to be appointed by agreement between the members of the fund, or a trade union or other organization representing the interests of the members and the employer or employers of those members, or an organization representing the interests of the employer or employers.⁴⁵⁷ If the trustee was appointed by such an agreement, the trustee could not be removed from office except as specified in the trust deed or as determined in the agreement.⁴⁵⁸

⁴⁵³ Ibid reg 13(g).

⁴⁵⁴ ISC Circular No 5 [24].

⁴⁵⁵ *OSSR* reg 14.

⁴⁵⁶ *OSSR* reg 15(1)(a)(i).

⁴⁵⁷ *OSSR* reg 15(1)(a)(ii).

⁴⁵⁸ *OSSR* reg 15(b).

If a body corporate was appointed as trustee of a small fund, equal representation was not required.⁴⁵⁹

If a vacancy occurred in the trustee or the board or committee that exercised control over the policies of the fund, the vacancy had to be filled within 60 days.⁴⁶⁰ The *OSSR* made no allowance for a reduction in the numbers of directors once that number had been established.

The operating standards that applied to the appointment of those responsible for the policies of the superannuation funds provided a mechanism of protection for members' benefits by ensuring the implementation of those standards. It also provided a deterrent for any potential conflict of interest by employers attempting to influence the decision making process.

6.7.4 *Review and regulate records*

6.7.4.1 *Audit*

The requirement for an independent auditor⁴⁶¹ continued under the operating standards in relation to the financial reports to be prepared regarding superannuation funds in *OSSA*.⁴⁶² The accounts and records of superannuation funds had to be audited by an 'approved auditor'⁴⁶³ each year with an auditor's report being given to the trustees.⁴⁶⁴ The auditor had to complete the auditor's certificate as prescribed by the *OSSR*.⁴⁶⁵

⁴⁵⁹ *OSSR* reg 15(2).

⁴⁶⁰ *OSSR* reg 15(1)(c).

⁴⁶¹ See above n 23.

⁴⁶² From 1 July 1982, an independent audit was required every year in the case of a loan back fund, and every three years in the case of other funds, to provide a certificate verifying the assets of the fund.

⁴⁶³ *OSSA* s 3(1), *OSSR* reg 4.

⁴⁶⁴ *OSSR* reg 17(1)(c).

⁴⁶⁵ *OSSA* s 12(1), Form 2 of Schedule.

An ‘approved auditor’ was defined as ‘a person registered as an auditor, or deemed to be registered as an auditor, under the Companies Act 1981 or a law of the State or Territory relating to companies’.⁴⁶⁶ An auditor was not regarded as ‘independent’ where there was a relationship with the superannuation fund. These relationships included where the auditor was:

1. a trustee or member of the fund, or a contributor to the fund;
2. a member of a management board, committee or other body having control over the policies of the fund;
3. a person having control over the investments or administration of the fund;
4. a partner, employee, or officer of a person associated with the fund outlined in above.⁴⁶⁷

The Auditing Standards Board issued the Auditing Guidance Release⁴⁶⁸ relating to the auditing standards of superannuation funds and ADFs. Three main topics addressed were:

1. the independence of auditors;
2. compliance with the *OSSR*, and
3. the reporting requirements.

The Certificate in the prescribed forms⁴⁶⁹ of the *OSSR* allowed an auditor to qualify the report:

1. the accounts of the fund could be qualified;
2. the auditor might have found evidence suggesting that the fund had not complied with the relevant prescribed standard during the year.⁴⁷⁰

⁴⁶⁶ *OSSR* reg (3)(1).

⁴⁶⁷ *OSSR* reg 4(3); ISC Circular No 6 [1]-[5].

⁴⁶⁸ Auditing Guidance Release (‘AUG’) No 5 first issued in October 1988, reissued in March 1990.

⁴⁶⁹ *OSSR* Schedule 1, Form 2 – superannuation funds; Form 3 – approved deposit funds; Form 3 – pooled superannuation trusts.

The auditor was not required to be an independent registered auditor if:

1. all assets were in the form of life policies or deposits at call with an eligible bank; or
2. the superannuation fund had 5 members or less, and those members agreed not to require a registered auditor.⁴⁷¹

The ISC could provide an exemption from the need to lodge audited ISC Annual Returns. This was available for the merger of small superannuation funds into master funds in respect of the part of the year of income during which the merger was effected. Compliance with set procedures for the application of the exemption was required.⁴⁷²

6.7.4.2 Actuarial investigation

Subject to transitional regulations,⁴⁷³ ‘defined benefit superannuation fund’⁴⁷⁴ had to have an actuarial⁴⁷⁵ investigation at least every three years.⁴⁷⁶ This requirement applied to public sector funds from 1 July 1990. Public sector funds fell into two categories:

1. fully funded superannuation funds;
2. not fully funded superannuation funds.

⁴⁷⁰ OSSR Form 2 of Schedule 1. The auditor certificate did not allow for any qualifications by the auditor prior to 21 October 1988. ISC Circular No 6 [15]-[17].

⁴⁷¹ OSSR reg 4(b).

⁴⁷² ISC Circular No 16, issued May 1990.

⁴⁷³ OSSR reg 17(a)(i), (ii).

⁴⁷⁴ OSSR reg 3(1) (definition of ‘defined benefit’ to be a superannuation fund whose trust deed provided that, for one or more members of the fund, the benefit on retirement from the workforce was defined in relation either to the member’s salary or to a specified amount).

⁴⁷⁵ OSSR reg 3(1) (definition of an ‘actuary’ to be a ‘Fellow or an Accredited Member of The Institute of Actuaries of Australia).

⁴⁷⁶ OSSR reg 17(i); ISC Circular No 8 [79]-[81]. Also the fund had to be unallocated, ie the contributions and investment earnings are not allocated to individual members, but are accumulated in a pool, out of which the benefits, calculated in accordance with the provisions of the trust deed, were paid.

A 'fully funded fund' was:

a defined benefit superannuation fund that is funded in advance in accordance with actuarial advice at a level that is intended to be reasonably adequate to provide for present and prospective liabilities in respect of benefits relating to the fund.⁴⁷⁷

For a private sector fund or a fully funded public sector fund, the actuarial report had to provide statements:

1. of the value of the assets of the fund;
2. of the actuary's opinion as to whether the value of the assets was adequate to meet the liabilities of the vested benefits in the fund;
3. of the recommended rate or rates of contribution by the employer over the following three years; and
4. whether the expected liabilities of the fund during the period of three years and the benefits that could reasonably be expected to vest at the end of that period for persons who were members of the fund could reasonably be met from:
 - (i) the value of the assets of the fund at the date of the latest valuation;
 - (ii) the assumed member contributions during the period of three years;
 - (iii) the assumed employer contributions during that period, calculated at the recommended rates; and
 - (iv) the earnings of the fund assumed by the actuary for the period.⁴⁷⁸

For a public sector fund that was not fully funded, the actuarial report had to include the following statements of:

1. the assets of the fund; and
2. any liability for benefit payments which was not expected to be covered by:

⁴⁷⁷ OSSR reg 3(1).

⁴⁷⁸ OSSR reg 17(2).

- (i) the assets of the fund; or
- (ii) any future contributions to, or earnings of, the fund; or
- (iii) a guarantee by the government or other body that established the fund; or
- (iv) an appropriation in respect of the fund.⁴⁷⁹

The certificate specified the minimum rate (or rates) of contribution required for each employer contributing to the fund in each year of income of the fund.⁴⁸⁰ This rate set out the minimum contributions required for the fund's assets to be reasonably regarded as sufficient to pay the minimum requisite benefits of all fund members. The calculation was to account for prior ranking liabilities and operating costs.⁴⁸¹

A certificate was normally for a five year period. It was required to be renewed for subsequent five year periods at least 12 months before its expiry.⁴⁸² If an actuary was not able to issue a five year certificate, the trustee might obtain a twelve month certificate.⁴⁸³ Reasons had to be supplied by the actuary for not issuing a five year certificate and what action needed to be taken.⁴⁸⁴ The trustee of a superannuation fund had to replace the 12 month certificate at least 3 months before its expiry and have written approval of the ISC to obtain a third or subsequent 12 month certificate.⁴⁸⁵

The process of auditing for accuracy of records and having actuarial investigations confirm the adequacy of assets for payment and quantum of members' benefits added to the transparency and credibility of the superannuation funds records.

⁴⁷⁹ *OSSR* reg 17(3).

⁴⁸⁰ *OSSR* reg 18U(1)(b).

⁴⁸¹ *Ibid.*

⁴⁸² *OSSR* reg 18U(2)-(4).

⁴⁸³ *OSSR* reg 18V(1).

⁴⁸⁴ *OSSR* regs 18V((3), (4).

⁴⁸⁵ *OSSR* regs 18V(5), (6).

The confidence in the superannuation system encouraged people to invest and save for retirement. The processes also provided a mechanism to ensure members' entitlements were available when required.

6.7.5 Report and disclose information

6.7.5.1 Reporting to the ISC

The trustees of superannuation funds had to provide information each year in a prescribed format ('annual ISC return') to the Commissioner.⁴⁸⁶ Two certificates had to be completed and incorporated in the return.⁴⁸⁷ The first certificate was a certificate validating the return and certifying that, with any exceptions noted, the fund return complied with the conditions that applied to it for the year.⁴⁸⁸ The second certificate was an audit certificate certifying that an audit had been conducted in accordance with the Australian Auditing Standards and that the information provided by the trustees was consistent with the audited accounts and records.⁴⁸⁹

The Commissioner could request by notice in writing that the trustees provide or report on specific matters specified in the notice.⁴⁹⁰ Also, the trustee might be required to produce relevant documents.⁴⁹¹ Non-compliance with the request to provide documents could result in the prosecution of the trustees by the Commissioner.⁴⁹² Prosecution had no effect on the eligibility for concessional tax treatment for superannuation funds. However, an

⁴⁸⁶ OSSA ss 10(1), 12(1)(a). The ISC could reject a return not lodged on an approved form for the relevant year. The Administrative Appeals Tribunal could not review such a decision. *Re Trustees of C & M Baldwin Pension Fund and the ISC*, 92 ATC 2063.

⁴⁸⁷ OSSA s 12(1)(b).

⁴⁸⁸ OSSA s 12(1); OSSR 24(1), Schedule 1 Form 1.

⁴⁸⁹ OSSA s 12(1); OSSR 24(2), Schedule 1 Form 2. See [5.7.4.1.2].

⁴⁹⁰ OSSA s 10(2).

⁴⁹¹ OSSA s 11.

⁴⁹² *Taxation Administration Act 1953*, s 8AA, 8C.

underlying issue might have resulted in all requirements not being satisfied and the fund not qualifying for concessional tax treatment.

6.7.5.2 Reporting to members

As part of protecting members' benefits, the OSSR included regulations to advise members of information pertinent to their ability to assess their investment and plan for their retirement.

6.7.5.2.1 Amendment to governing rules

The trustee of a superannuation fund had to provide to each member, as soon as practicable⁴⁹³, a written statement explaining the nature and purpose of an alteration and the effect (if any) of the alteration on the entitlements of its members.⁴⁹⁴

This operating standard was subsequently altered requiring the advice of an alteration to the trust governing rules be given as soon as practicable to those members who had been or potentially could be affected by the alteration.⁴⁹⁵

An additional requirement applied to all funds with five or more members from 1 July 1992. If the governing rules of the fund were to be altered in such a way as to increase the entitlement of a member who was also the employer or an associate of the

⁴⁹³ ISC Circular No 8 [94], October 1988, stated that 'as soon as practicable' meant:

- where alterations affect accrued entitlements or the basis of calculating those benefits, they should be notified to members immediately; or
- where such alterations:
 - do not affect those entitlements, or
 - while they may affect those entitlements, are made only:
 - to reflect the effect of the introduction of tax on superannuation contributions or earnings, or
 - to comply with the operational standards, including the reasonable benefits limits,

they could be notified at the next available opportunity, eg at the time of the annual report to members.

⁴⁹⁴ OSSR reg 17(1)(h).

⁴⁹⁵ OSSR reg 18E(2)(a). as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulation (Amendment)*, Statutory Rules 1992 No 224, 30 June 1992. ISC Circular No 28 [46].

employer, that proposal had to be advised to fund members at least three months before the change was to take effect.⁴⁹⁶

6.7.5.2.2 Regular reports

Prior to 1 July 1992, the original regulations in the OSSR provided the following requirements for disclosing information to members⁴⁹⁷:

1. a statement to a new member set out:
 - (i) the details of the kinds of benefits;
 - (ii) the conditions relating to those benefits;
 - (iii) the method of determining entitlements of members.⁴⁹⁸
2. an annual statement to each member about the 'year of income' as soon as practicable after the end of that year but within six months.⁴⁹⁹
3. a statement to departing members:
 - (i) the amount of the member's benefit entitlement and the method of determining that entitlement;
 - (ii) any amount that had to be preserved as required by the OSSR or the trust deed;
 - (iii) where a person ceased to be a member otherwise than by death, disablement or retirement from the workforce, a statement containing the following information for the period from the end of the previous year of income of the fund up to the date when the member ceased to be a member:
 - benefits calculated on the basis of contributions made to the fund, with or without the addition of earnings on those contributions;

⁴⁹⁶ OSSR reg 18E(5)(b), as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulation (Amendment)*, Statutory Rules 1992 No 224, ISC Circular No 28 [45].

⁴⁹⁷ OSSR regs 17(1)(e)-(i). ISC Circulars No 5 [41]-[48], No 8 [28]-[30], [82]-[94], No 17 [16], [17], [38], No 20 [15]-[19].

⁴⁹⁸ OSSR reg 17(1)(g).

⁴⁹⁹ OSSR regs 17(1)(e); 17(4)-(5).

- benefits based on an endowment or whole of life policy; and
 - benefits defined in terms of the member's salary (or average salary).⁵⁰⁰
4. if requested by a member, a copy of
- (i) any statement given by an actuary;
 - (ii) the auditor's report;
 - (iii) the annual return given to the ISC; and
 - (iv) certificates and notices issued by the ISC.⁵⁰¹

From 1 July 1992, the operating standards for disclosure and reporting information to members of superannuation funds were significantly expanded.⁵⁰² The reason for the expansion was to introduce new standards which:

- made trustees and managers of superannuation funds more accountable to fund members by providing information on the investment strategy, earnings and costs of the fund; and
- provide better information to members of superannuation funds about the operation of their fund so that they might better evaluate the fund's performance.⁵⁰³

The operating standards required the trustees of all superannuation funds to provide information in the following circumstances:

- when members (or before prospective members) join the fund;⁵⁰⁴

⁵⁰⁰ OSSR reg 17(1)(f).

⁵⁰¹ OSSR reg 17(1)(i).

⁵⁰² The Treasurer, John Kerin M P, '1991/1992 Federal Budget' (Speech to the House of Representatives, Canberra, 20 August 1991).

⁵⁰³ The Treasurer, John Kerin, M P, 'Prudential Supervision of the Supervision Industry', Press Release No 73, 20 August 1991. The Federal Government's policy statement on prudential supervision of the superannuation industry: Paper 1 'Review of Supervisory Framework for the Superannuation industry', Paper 2 'Occupational Superannuation Standards (OSS) Regulations Disclosure of Information to Members of Superannuation Funds'. 20 August 1991.

⁵⁰⁴ OSSR reg 18E.

- when members leave the fund;⁵⁰⁵
- when requested by members;⁵⁰⁶
- when alterations were made to the fund's trust deed;⁵⁰⁷ and
- regular reporting for a reporting period⁵⁰⁸ to members concerning their benefit entitlements (ie the provision of a benefit statement to each member).⁵⁰⁹

The introduction of these operating standards introduced the concept of different reporting for superannuation funds with different numbers of members. A multi-member superannuation fund was one which:

- had more than four members; and
- did not rely entirely on the terms of life insurance policies⁵¹⁰ to define the benefit entitlements of its members.⁵¹¹

505 *OSSR* reg 18F.

506 *OSSR* regs 18L, 18G.

507 *OSSR* reg 18E(2)(a).

508 *OSSR* reg 18C(1) (definition of 'reporting period' to mean 'a period of not more than 12 months').

509 *OSSR* reg 18G.

510 *Life Insurance Act 1945* s 4 (definition of 'life insurance policy' as 'a policy insuring payment of money on death (not being death by accident or specified sickness only) or on the happening of any contingency dependent on the termination or continuance of human life').

511 *OSSR* reg 18C(1).

The following table prepared by the ISC⁵¹² set out a summary of the substituted reporting and disclosure of information requirements in the OSSR.

	Regular reports	On request	On exit	New members	Return of fund money to employer sponsor	Change to fund governing rules
Funds with five or more members and with employer sponsor	18G, 18H	18L, 18M	18F	18E(2)(c), 18E(3)(c)(ii), 18E(3)(e) if individual member accounts kept	18E(5)	18E(2)(a)
Funds with five or more members and without employer sponsor	18G, 18H	18L, 18M	18F	18E(2)(b), 18E(3)(c)(i), 18E(3)(d) if individual members accounts kept, 18E(3)(f) if not subject to prospectus requirements of the Corporations Law and not affected by circulars to life companies.	18E(5)	18E(2)(a)
All other funds with employer sponsor	18G	18L	18E(2)(c)	18E(2)(c)	N/A	18E(2)(a)
All other funds without employer sponsor	18G	18L	18F	18E(2)(b)	N/A	18E(2)(a)

Table 10: Information to be given to members⁵¹³

6.7.5.3 Prospectus requirements

On 24 February 1993, the OSSR included requirements for prospectus content⁵¹⁴ which had previously been applied under the Corporations Law.⁵¹⁵ This resulted from the Treasurer's announcement that the ISC was to be the sole regulator of the

⁵¹² ISC Circular No 28 Attachment A, July 1992.

⁵¹³ CCH Australia Limited, *The Superannuation Legislation*, (February 1993), [35-187].

⁵¹⁴ OSSR reg 5AAA, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1993 No 33 17 February 1993, ISC Circular No 32, February 1993. OSSR reg 5AAA later repealed. OSSR regs 5AAA AAB, AAC, AAD, as inserted by Commonwealth of Australia, *Occupational Superannuation Standards Regulations (Amendment)*, Statutory Rules 1993 No 213, 27 July 1993, 6.

⁵¹⁵ *Corporations Act 1990* ss 66A, 1017, *Corporations Regulations* regs 7.12.05(c), 7.12.06(d).

superannuation industry.⁵¹⁶

The *OSSR* required that not only must a prospectus be lodged with the ISC, but also be registered by the ISC. Registration depended on vetting procedures by the ISC to ensure that it complied with the *OSSR*'s prescribed conditions.⁵¹⁷ The ISC set out the guidelines that a prospectus had to meet. These included:

- there must be full disclosure of risk factors with advice of any disadvantages, for example, the fact that a person may outlive an allocated pension;
- definitions must be accurate and meet the minimum requirements of the OSS legislation, for example, the definition of permanent incapacity and disability;
- borrowings and contribution provisions must be consistent with the OSS legislation, for example, members' assets, contributions in specie;
- the prospectus must include current financial statements with comparative figures for the previous year where relevant;
- the prospectus must advise the expected time the fund will take to pay benefits;
- there must be a disclosure of the level of fees;
- the source of any external statistical data must be stated;
- ...⁵¹⁸

The ISC had the discretion to modify or exempt a superannuation fund from having to comply with the prospectus standards by way of a determination.⁵¹⁹

The reporting and disclosure requirements in the *OSSR* provided a mechanism for the ISC to review the operations of a fund and its management by the trustees. The requirement in the *OSSR* to report and disclose information to members attempted to make the

⁵¹⁶ The Treasurer, the Hon John Dawkins M P, *Strengthening Super Security, New Prudential Arrangements for Superannuation* (Australian Government Publishing Services 1992) 2.

⁵¹⁷ ISC Circular No 37 [35]-[38] August 1993.

⁵¹⁸ Ibid [38].

⁵¹⁹ *OSSA* s 12A.

members fully informed so that they could evaluate their investment and plan for retirement. Both processes provided transparency and allowed reviews of the operations of the fund by the ISC and the members. The integrity of the system was essential for members' confidence and to encourage their saving for retirement.

6.8 Decision reviews and challenges

Reviews of decisions⁵²⁰ by the Administrative Appeal Tribunal ('AAT')⁵²¹ and challenges by various parties highlighted inadequacies in the *OSSA* and *OSSR*.

6.8.1 The trustee of superannuation funds

The Commissioner of the ISC would give a notice to the trustee of a superannuation fund where the Commissioner was satisfied that the superannuation fund complied with the conditions in relation to the year of income, having regard to:

- (a) the return and certificates given to the Commissioner; and
- (b) any other information available to the Commissioner.

If a notice was given to the trustee of a superannuation fund stating that the Commissioner was not satisfied that the fund complied with fund conditions in relation to a year of income, the notice had to set out the reasons for the decision.⁵²² The Commissioner of the ISC advised the Commissioner of Taxation of all notices given to the trustee of a superannuation fund.⁵²³ If a notice of non-compliance was issued, the Commissioner of

⁵²⁰ *OSSA* s 3(1) (definition of 'reviewable decision' included decisions made under *OSSA* s 12A).

⁵²¹ *OSSA* s 16(6).

⁵²² *OSSA* s 12 (7).

⁵²³ *OSSA* s 12(8).

Taxation would not apply the concessional tax rate to the superannuation fund.⁵²⁴

The trustees of superannuation funds could request the AAT to review the decision of the Commissioner of the ISC.

6.8.1.1 Sole purpose

Some of the principles of the sole purpose for establishing and maintaining a superannuation fund were established before the introduction of the OSSA and OSSR. The incidental benefiting of a some party other than the employees or their dependants was thought not to be a breach of the sole purpose test.⁵²⁵

In the ‘Swiss chalet case’⁵²⁶, providing benefits for the recreational use of employees and personal use by the directors of the employer sponsor was considered to breach the sole purpose test. Denying access to members about the superannuation fund and their possible future entitlements supported the argument that the superannuation fund was not maintained for the employees. The AAT found that the superannuation fund did not comply with the definition of ‘superannuation fund’.⁵²⁷

6.8.1.2 Investment Standards

The restriction against borrowing⁵²⁸ and lending⁵²⁹ was included in the regulations as an investment standard. The operating standards relating to borrowing and lending by the trustees of superannuation funds were mostly unambiguous but did require

⁵²⁴ ITAA s 23FC to 30 June 1988; from 1 July 1988, ITAA pt IX.

⁵²⁵ *Rollason v FC of T* (1966) 121 CLR 45; *Compton v FC of T* (1965) 116 CLR 233; *Case X60 90 ATC 438*; *Case 23/96 96 ATC 278*.

⁵²⁶ *Case 43/95 95 ATC 394*.

⁵²⁷ OSSA s 3(1).

⁵²⁸ OSSR reg 16(1)(b).

⁵²⁹ OSSR reg 16(1)(a).

minor interpretation.⁵³⁰ Any defence to the ISC's providing a notice of non-compliance usually depended on the Commissioner failing to exercise the discretion to treat the fund as complying.⁵³¹

The provisions in the *ITAA* relating to the in-house asset rules were imprecise and required interpretation. The lack of clarity resulted in the provisions for compliance being transferred to the *OSSR*. The new regulation attempted to clarify the application of the rules.⁵³² There remained a number of terms that needed interpretation and clarification.

The interpretation of an in-house asset depended on the definition of what was an associate of an employer sponsor, defined in the *ITAA*. See Chapter 3 [3.1.1.3] for the discussion on the definition and the possible applications. The definition of an 'associate'⁵³³ of an employer sponsor of the fund provided a method of investment not intended.⁵³⁴ For example, the use of a unit trust as an investment vehicle became an accepted practice. This circumvented the provisions that prohibited superannuation fund borrowing or lending.

The term 'financial link in relation to an employer sponsor of the fund' in relation to the application of what constituted an in-house asset lacked clarity and raised the question of what assets were to be included in the in-house asset calculation.⁵³⁵ Where an asset

⁵³⁰ *Case Z27 92* ATC 255: breach the *OSSR* reg 16(1)(b), (5) relating to 'temporary finance'. *Case 17/94 94* ATC 198; *Case 54/94 94* ATC 472; *Case 71/96 96* ATC 635: breach *OSSR* reg 16(1)(b) relating to unauthorised borrowings. *Case 14/95 95* ATC 189: breach *OSSR* reg 16(1)(a) relating to lending to members of the fund.

⁵³¹ See below [6.8.1.3].

⁵³² See above n 407.

⁵³³ *ITAA* s 26AAB(14).

⁵³⁴ *Case 5/94 94* ATC 130; *Case X70 90* ATC 537, appealed *Trevisan (Trustees of Forli Pty Limited Superannuation Fund) v FC of T* 91 ATC 4416; *Case Y55 91* ATC 474; *Case 23/96 96* ATC 278; *Case 56/94 94* ATC 484 appealed *ISC v Hiscock as trustee for Osborne Fruit Drinks Superannuation Fund* 95 ATC 4575; *Case 71/96 96* ATC 635.

⁵³⁵ *OSSR* reg 16A(9).

was acquired without consideration, the cost of the asset for the purposes of the calculation of in-house assets was at a cost that the Commissioner was satisfied as ‘reasonable in the circumstances’.

6.8.1.3 *Special circumstances discretion*

The Commissioner of the ISC could exercise his discretion to treat a superannuation fund as complying in a particular year even though it had failed to do so and was not entitled to a notice that it had complied.⁵³⁶ The trustee of the superannuation fund had to satisfy the Commissioner of the ISC that special circumstances existed in relation to the year in question, making it reasonable to treat the superannuation fund as if it had complied with the superannuation conditions for that year.⁵³⁷ The imprecise language in s 13 of the O SSA, inter alia, was relied upon by trustees of superannuation funds in their defence when their fund was not issued with a notice of compliance.⁵³⁸

The ISC Guidelines outlined the factors to be taken into account by the ISC in determining if special circumstances existed which

⁵³⁶ O SSA ss 12, 13.

⁵³⁷ O SSA s 13(1)(b).

⁵³⁸ *Case Z27 92 ATC 255, Case 54/94 94 ATC 472: breach OSSR reg 16(1)(b), (5) relating to ‘temporary finance’.*
Case 17/94 94 ATC 198; Case 54/94 94 ATC 472: breach OSSR reg 16(1)(b) relating to unauthorised borrowings.
Case 14/95 95 ATC 189: breach OSSR reg 16(1)(a) relating to lending to members of the fund.
Case 4/95 95 ATC 119: breach OSSR reg 16(3), failing to comply with borrowing standards as soon as practicable.
Case 33/94 ATC 306; Case 47/94 94 ATC 417; Case 43/95 95 ATC 394; Case Y55 91 ATC 474; Case 23/96 96 ATC 278; Case 71/96 96 ATC 635: breach OSSR reg 16, 16A ‘in-house asset rule’.
Case 33/94 94 ATC 306; Case 11/95 95 ATC 173, Case 23/96 96 ATC 278, Case 28/96 96 ATC 327; breach OSSR reg 16(1)(b), ignorance of the law, incorrect legal and accounting advice, audit delay or Commissioner’s delay not ‘special circumstances’.
Case 56/94 94 ATC 484: breach OSSR reg 12(3A), rectified and ISC advised as soon as practicable, remitted from the Federal Court (ISC v Hiscock as trustee for Osborne Fruit Drinks Superannuation Fund) 95 ATC 4575: meaning of ‘special circumstances’, Case 73/96 96 ATC 653, AAT set ISC’s decision aside.

would make it reasonable to treat a superannuation fund as having satisfied the OSSA and OSSR. These included:

- the particular standard(s) breached;
- the degree of the breach of the standards;
- the effects of the breach on the long-term retirement interests of the members;
- whether the trustees knew of the breach and took steps to rectify it;
- claims that the breach would be rectified;
- claims that the trustees had received incorrect professional or Departmental advice;
- whether the trustees took any action to remedy breaches after they became aware of the incorrect advice provided;
- practical difficulties faced by trustees in seeking to comply with the standards;
- impossibility of complying with the standards; and
- ignorance or misunderstanding of the nature of the standards.⁵³⁹

In *Case Z27*⁵⁴⁰, the Tribunal stated that the courts and the Administrative Appeals Tribunal had been strict in their interpretation of 'special circumstance'. It summarised the questions for the application of the Commissioner exercising the discretions relating to 'special circumstances':

The following strict tests should therefore be applied by a decision-maker in assessing whether the circumstances claimed by the trustees in a particular case are 'special circumstances'. In other words, most of the following questions should be answered in the affirmative if the discretion is to be exercised favourably –

- (a) are there factors existing which would justify the making of an exception to the general rule that if there is a breach of standards, a notice of compliance is to issue;

⁵³⁹ CCH Australia Limited, *Superannuation Law Practice*, 1996, [34-320]. These guidelines were not published but obtained under the *Freedom of Information Act*.

⁵⁴⁰ *Case Z27 92* ATC 255 260.

- (b) are the circumstances advanced *unusual, uncommon, exceptional, abnormal* in character, quality or degree?
- (c) do the circumstances relating to the breach make it unjust, unreasonable or inappropriate to issue a Notice of Non-Compliance;
- (d) if there has been a *gross* departure from a standard or standards, are there *very weighty* special (unusual, uncommon, exceptional, abnormal) circumstances advanced;
- (e) have all the facts and circumstances been examined *together* and not in isolation. (This is important because what could constitute special circumstances in relation to one fund, may not constitute special circumstances regarding another fund, when taking into account all the circumstances of that other fund. It is important to keep an overview of all the facts of a matter);
- (f) is there an element of involuntariness in the breach or were external forces beyond the control of the fund present to cause the breach;
- (g) do the circumstances advanced as 'special' amount to much more than mere bad luck;
- (h) has the trustee evinced an intention to rectify the breach within a reasonably short period.

A review of the cases in which the defence relied on 'special circumstances' applying demonstrated that the Tribunal did apply the guidelines strictly and relied on the evidence provided. Whilst allowing the Commissioner of the ISC to exercise discretion to treat a superannuation fund as complying, it provided trustees of superannuation funds the right to challenge a decision that was not favourable. As it was the members and their benefits that suffered from a superannuation fund becoming non-complying and taxable, this right to challenge provided some protection for the members.

Superannuation funds that were non-complying were penalised by the imposition of non-concessional rates of tax on the superannuation funds. This in turn affected members' benefits. Under the *OSSA* and *OSSR*, there was no right for a member to seek damages from the trustees when the latter had been

negligent. The Commissioner of the ISC was unable to prosecute the trustees for negligent actions except where they had failed to respond to a request for documents.

6.8.2 *The trustee in bankruptcy*

A trustee in bankruptcy challenged the trustee of a superannuation fund on the basis that a member's vested benefits should be vested in the trustee in bankruptcy.

The question of vesting and preservation in the event of bankruptcy of a member was addressed in the landmark case of *Re Bond; Ex Parte Ramsay*.⁵⁴¹ Also raised was the question of whether the clause in the trust deed relating to forfeiting benefits in the case where an act of bankruptcy had been committed by a member of the fund was valid. On the facts of this case, it was held that the member's benefits had vested due to the particular circumstances but some part of that benefit may be required by the OSSR to be preserved. In this case, the forfeiture clause in the trust deed was found to be void and inoperative. An appeal to the Full Federal Court was dismissed.⁵⁴²

This case exposed issues in the OSSR that made a member's benefits vulnerable in the event of bankruptcy. This vulnerability undermined the protection that the vesting, preservation and portability of a member's benefits provided.

The issues identified exposed the members' benefits as well as the Revenue and needed to be resolved.

⁵⁴¹ 92 ATC 4807.

⁵⁴² *Caboche v Ramsay* 93 ATC 5135.

6.9 Conclusion

Having acknowledged the need for people to save for their own retirement, the Federal Government provided tax incentives for savings accumulated for retirement in superannuation funds. Initially, the tax incentive was exemption from income tax for the income of superannuation funds established for the benefit of employees. In 1961, investment in public securities was imposed on these superannuation funds, public sector funds excepted. Compliance with the investment requirement was essential for the superannuation fund to be eligible for its income to be exempt from income tax. In 1964, some restrictions for exemption were introduced on dividend income from private companies. The requirement for investment in public securities was abolished on 11 September 1984 and the in-house asset rules were introduced on 1 July 1985. Both of these amendments to the *ITAA* were recommendations by Committees.

In 1988, the income of superannuation funds became taxable but at concessional rates if the superannuation fund complied with the requirements of the *OSSA* and *OSSR*. The amount of assets accumulated in superannuation funds was \$32 billion in 1983. This coupled with the inevitable introduction of compulsory contributions in 1992 increased the concern to protect the superannuation fund assets and accentuated the need for a regulatory framework. On 23 October 1987, the Occupational Superannuation Standards Bill and other related legislation were passed by Parliament.

During the period that the Commissioner of Taxation was responsible for the regulation of superannuation funds, to further encourage savings by extending the availability of concessional tax treatment, the Federal Government developed different types of

superannuation funds to cater for people other than employees and those supported by employers.

During this time, the Commissioner disallowed the exemption of income of superannuation funds on the basis that they did not comply with the requirements of the *ITAA*. These challenges revealed specific inadequacies in the *ITAA* that made the Revenue vulnerable. They also highlighted the fact that members' benefits had no protection and the members had no rights. There were no restrictions on the use of the funds accumulated in superannuation funds. Unless there were restrictions within the trust deed governing the superannuation fund, the trustee could lend to the employer sponsor and their associates and members of the fund and the relatives, with or without security, with or without interest. The trustee could invest in the employer sponsor and borrow money using the superannuation fund's assets as collateral. Apart from the requirement for a member to be advised of the existence the right to a benefit, no further information had to be provided to a member in respect of his benefits.

The Federal Government appointed various Committees to examine the legislation that regulated superannuation funds and to identify any anomalies, inconsistencies and unnecessary complexities. The Reports relevant to the regulation of superannuation funds, identified by the names by which they became known, were:

1. the Ligertwood Report, reported June 1961
2. the Asprey Report, reported January 1975;
3. the Hancock Report, reported March 1977;
4. the Campbell Report, reported September 1981; and
5. the Task Force, reported January 1983.

The Committees formulated proposals to remedy the identified inadequacies. Whilst the maintenance of the Revenue was a prime concern, the Federal Government policy to encourage people to

save for their own retirement and to protect these savings to ensure that they were available when required was also of paramount importance. There was bi-partisan support for the retirement policy. The finalisation of the plan adopted by the Federal Government took a number of Reports and many years. The initial introduction of the *OSSA* and *OSSR* in 1987 provided the framework for the regulation of superannuation funds. The framework and operating standards were based on the Reports, especially that of the Task Force. The provisions of the *OSSA* incorporated the principles identified by the courts. Both the *OSSA* and *OSSR* were amended as required to clarify the application of the provisions and regulations and insert new provisions and regulations to develop the regulation to provide the protection for members' benefits.

The establishment of the Insurance and Superannuation Commission provided a new regulatory authority to supervise superannuation industry. The inclusion of the public sector funds within its jurisdiction progressed the consolidation process of regulation.

The adoption of one category of superannuation fund (foreign superannuation funds excepted) dispensed with the diversity of superannuation funds and regulations that applied to those funds.

The sole purpose of a superannuation fund being established and maintained for retirement, adopted as an essential requirement, dictated the content of the operating standards.

The *OSSA* and *OSSR* protected members' benefits by providing a mechanism for identifying and quantifying a member's benefits, vesting and preserving those benefits and by allowing the member to relocate the benefits if employment was changed. It restricted

the use of members' benefits and the assets of the superannuation fund.

Detailed information about the operation of the superannuation fund being provided to the ISC and members added to the transparency of the operations of the superannuation fund. The regulation for the composition of the trustees or board of a corporate trustee or management ensured that the members and the employers were represented and their interests were protected. It also reduced the possibility of any conflict of interest for the trustees. The auditing and actuarial investigation requirements provided integrity to the accounting and adequacy of members' benefits. The supervision of the regulation of the superannuation industry by the ISC inspired confidence for members.

It was thought unnecessary to make trustees accountable for their responsibilities by imposing penalties on them. The threat to loss of concessional tax status by the superannuation was considered sufficient motivation for compliance. It seems that the decision not to include provisions for penalties for non-compliance with the O SSA and O SSR was probably due to the uncertainty of the scope under the *Constitution* for the Federal Government to legislate for this. The Federal Government missed an opportunity to resolve the issue posed by the *Constitution* and the imposition of penalties. Had this been addressed and resolved, the introduction of the O SSA and O SSR, its having to be repealed and replaced by the SISA may not have been necessary. The Federal Government's staged introduction of the amendments to the regulation of superannuation funds was appropriate. The overall changes to the superannuation industry were radical and required careful implementation.

The introduction of the O SSA and O SSR included the recommendations of the Committees. It was consistent with the

Federal Government's policy intent to encourage people to save for their own retirement and protect members' benefits.

Further issues of clarity of language and terms used were identified in reviews of ISC decisions by the AAT and remained to be addressed. There also remained the duplication of the supervision of processes by different authorities. The ISC and ASC supervised fund raising, the issuing of Prospectus and reporting. Making trustees accountable for their responsibilities and additional means to prevent abuse of the superannuation had to be addressed.

This Chapter has shown that the Federal Government recognised the inadequacies in the regulation in protecting members' benefits and ensuring the accountability of trustee. The *OSSA* and *OSSR* were introduced. Chapter 7 will analyse their effectiveness.

CHAPTER 7

SUPERANNUATION INDUSTRY (SUPERVISION) ACT 1993

Chapter 2 discussed the initial structure of superannuation funds when the Australian Taxation Office ('ATO') regulated them. It then examined the evolution of the superannuation fund/trust into the 'statutory' trust. Chapter 3 detailed the progress of the taxation of income of superannuation funds from exemption from tax provided there was compliance with the provisions of the *Income Tax Assessment Act 1936* ('ITAA') to concessional treatment, again subject to compliance. Chapters 4 and 5 outlined and analysed the superannuation funds developed to provide an effective mechanism to allow and encourage people to save for their retirement. The analyses of these chapters established the inadequacies and anomalies in the legislation that were identified by the challenges by the Commissioner of Taxation at the Board of Review and the Courts. The various Committees appointed by the Federal Government to review the taxation system, including the taxation of superannuation funds and the parties associated with the funds, confirmed these inadequacies and anomalies. Chapter 6 reviewed the various reports from those Committees. It demonstrated that the Federal Government relied on these reports in developing strategies to implement their retirement income policies. The legislation introduced for the regulation of superannuation funds was the *Occupation Superannuation Standards Act 1987* ('OSSA') and its Regulations ('OSSR'). A discussion of the issues that caused the trustee of superannuation funds to request the Administrative Appeals Tribunal ('AAT') to review decisions of the Commissioner of the Insurance and Superannuation Commission ('ISC') exposed the inadequacies that remained in the provisions of the OSSA and the OSSR and that allowed members' benefits to be vulnerable and not secure.

Chapter 7 analyses the reports to the Federal Government on the effectiveness of the *OSSA* and *OSSR* that resulted in the introduction of the *Superannuation Industry (Supervisions) Act 1993* ('*SISA*') and the Regulations ('*SISR*'), the legislation that replaced *OSSA* and *OSSR*. It outlines the operating standards established for the protection of members' benefits introduced in the *OSSA* and *OSSR* and incorporated into *SISA*, some without change and some amended to strengthen and provide clarity. Amendments to the provisions pertinent to the protection of members' benefits are identified and discussed.

This Chapter reviews the new measures introduced in the *SISA* for increased protection of members' benefits. These measures restricted those who could act as trustees. Provisions for trustees' obligations and duties for the operation of superannuation funds, previously in the legislation for trusts regulated by the various States and Territories, were included in the *SISA*. The imposition of penalties for non-compliance with the provisions of the *SISA* by the trustees was to protect the members' benefits. A mechanism for dispute resolution for members was introduced. Licensing of trustees was later introduced to enhance the quality and qualifications of those participating in this role.

The Chapter discusses the rationale for the establishment of a new regulator, the Australian Prudential Regulation Authority ('APRA') to replace the ISC and the introduction of the new type of superannuation fund, 'self managed superannuation fund'. As part of streamlining the regulation of the superannuation, the supervision of some procedures undertaken by the trustees was reassigned to rationalise the duplication of functions of the authorities. The *SISA* also provided anti-avoidance measures and penalties to prevent the abuse of accessing the concessions available to superannuation funds.

This chapter will discuss whether the legislation developed for the regulation of superannuation funds provided a framework that allows the Regulators to efficiently and effectively protect the members' benefits, makes the trustees accountable for their responsibilities and minimises the abuse of the superannuation system. It will consider if the evolution of the legislation regulating superannuation funds has been consistent with the Federal Government's policy intent to encourage people to save for their own retirement.

7.1 Background

Demographic and projected economic analysis since the beginning of the 20th century confirmed the need for affirmative action in providing funding for retirement.¹ To encourage people to save for their retirement, the Federal Government developed a range of superannuation funds to provide the opportunity for different sectors of the community to access tax concessions.²

During the 1970s and the early 1980s, Australia experienced an increase in the application of tax avoidance techniques, including accessing the exemption and concessional treatment of income by using the provisions relating to superannuation funds.³ To counteract this, the Federal Government introduced new legislation for the regulation and supervision of superannuation funds, ADFs and PSTs. The introduction of this legislation, the O SSA with the associated OSSR, included the need for the establishment of a new authority, the Insurance and

¹ See Chapter 1 [1.2].

² See Chapters 3, 4, 5.

³ Chapter 1 [1.4] n 79.

Superannuation Commission ('ISC') with a new statutory officer, the Insurance and Superannuation Commissioner.⁴

The O SSA and the OSSR provided substantial protection for members' benefits. These protections were discussed in Chapter 6.

In addition to complying with these provisions in the O SSA, the trustees had to comply with the general duties applicable to trustees included in the legislation of the States and Territories that applied to trustees. These duties included:

1. to observe the trust deed;⁵
2. to act in the best interest of members;⁶
3. not to derive a profit from the trust;⁷ and
4. to avoid a conflict of interest.⁸

Where the trustee was subject to the Corporations law⁹, eg a fund operated by a life insurance company, the additional regulation provided additional protection for members' benefits. The prudential requirements of the *Life Insurance Act 1945* also applied to funds operated by life assurance companies.¹⁰

The regulatory bodies responsible for the observance of the O SSA and the additional standards were:

1. ISC for O SSA;

⁴ Chapter 6.

⁵ H A J Ford and W A Lee, *Principles of the Law of Trusts* (The Law Book Company Limited 1983) 387 [908].

⁶ Ibid 388 [909].

⁷ Ibid 389 [910].

⁸ Ibid 399 [925].

⁹ Before 1981, Uniform Companies Act 1961.

After 1981, *Companies Code 1981* ('Companies Code' subject to and in accordance with the *Companies (Application of Laws) Act 1981*, *Companies and Securities (Interpretation and Miscellaneous Provisions) (Application of Laws) Act 1981*); from 2001 *Corporations Act 2001* ('CA').

¹⁰ See Chapter 5 [5.4].

2. Australian Securities Commission ('ASC') for ensuring that companies met their obligations under the Corporations Law; and
3. Reserve Bank for banks engaged in the superannuation industry.

Inadequacies identified in the O SSA and OSSR impeded the efficient supervision and regulation of superannuation funds, ADFs and PSTs. In addition to lack of clarity of language and terms in the O SSA, there was duplication of the supervisory functions and a lack of suitable remedies for breaches of the O SSA.¹¹

In February 1986, the Federal Government¹² commissioned a review of social security policy focusing on three major aspects:

- income support for families with children;
- social security and workforce issues; and
- income support for older people.¹³

The Social Security Review¹⁴ was released in 1988. It confirmed the projected demographics relating to the ageing of the population.¹⁵ It included the issue of income support for older people and the need for changes to achieve more adequate retirement income through better integration of the pension, superannuation and tax systems.¹⁶ An objective of the Social Security Review relating to the income support for older people was to propose directions for long-term reform.¹⁷ It suggested that the following initiatives were necessary to improve the interactions of age pension and

¹¹ See Chapter 6 [6.8].

¹² The Australian Labor Party government under the Prime Minister Rt Hon Robert James Hawke, AC.

¹³ See below n 14, i.

¹⁴ Social Security Review *Towards a National Retirement Incomes Policy* (Issues Paper No 6 Commonwealth of Australia, 1988).

¹⁵ Ibid 56.

¹⁶ Ibid 101, 199-203.

¹⁷ Ibid iii.

superannuation and to ensure that government support of retirement income was made more cost effective and equitable:

1. measures to improve vesting¹⁸;
2. measures to ensure greater preservation of superannuation entitlements to genuine retirements,¹⁹ including a higher preservation age²⁰;
3. an increased trend towards superannuation benefits being taken in pension or annuity form;²¹ and
4. further extension of the coverage of superannuation to ensure that government support provided through its superannuation policy was more widely spread.²²

Each of these proposed initiatives supported the Federal Government's policy. They encouraged people to save for their own retirement by indicating to the people the Federal Government's intent to support their efforts by extending the coverage of superannuation and by improving the vesting and preservation provisions. The proposal for taking superannuation benefits as a pension or annuity reflected the Federal Government's policy to provide income for retirement.

The Federal Government claimed that its policies of encouraging superannuation had been successful.²³ The assets in superannuation funds increased from \$32 billion in 1983 to \$125 billion by December 1990. The Treasurer stated that:

Official encouragement of superannuation savings brings with it an obligation on Government to provide an appropriate prudential framework. The government will therefore be placing increased emphasis

¹⁸ Ibid 138, 161, 188, 202.

¹⁹ Ibid.

²⁰ Ibid 185, 201.

²¹ Ibid 153, 190-2, 202.

²² Ibid 161, 188, 202.

²³ The Treasurer, John Kerin MP 'Prudential Supervision of the Superannuation Industry', (Press Release No 73, 20 August 1991).

on the accountability, financial stability and efficiency of the superannuation industry.²⁴

With the proposed introduction of compulsory superannuation²⁵ and the continuation of tax incentives provided to encourage people to save for their retirement, the amount under the control of superannuation funds was expected to continue to increase. By the turn of the century, the assets in superannuation funds were estimated to increase to between \$300 and \$600 billion.²⁶ However, members' benefits were seen to be at risk from trustees losing large amounts of money. This expected increase in the size of superannuation funds and the diverse range of funds operating²⁷ resulted in the Federal Government's reviewing the regulation of the superannuation industry again.

On 20 August 1991, the Treasurer announced the release of two papers outlining the Federal Government's approach to increasing the prudential standards relating to superannuation funds.²⁸ The first outlined the measures to be implemented to provide adequate prudential framework to improve the security of funds invested in superannuation. Whilst it was not the Federal Government's intention to guarantee superannuation funds, it announced that it would minimise risks by making trustees subject to legislative controls relating to their fiduciary responsibilities and accountability.²⁹ The second paper outlined the requirements for improving the accountability and efficiency of superannuation funds. These additional requirements were to provide greater

²⁴ Ibid.

²⁵ The decision to introduce a Superannuation Guarantee Scheme ('SGS') was announced in the 1991-1992 Budget.

²⁶ The Treasurer, John Kerin MP 'Review of Supervisory Framework for the Superannuation Industry' Paper 1 released 20 August 1991 1 [3].

²⁷ Ibid 3 [11].

²⁸ See above n 23.

²⁹ Paper 1 'Review of Supervisory Framework for the Superannuation Industry'.

protection to members by making trustees and fund managers more accountable by providing information on the investment strategy, earnings and costs of the fund. They were to be included in the *OSSR* and to apply to all superannuation funds with 5 or more members.³⁰

After the *OSSA*, the evolution of the legislation regulating superannuation funds, ADFs and PSTs ('superannuation entities') to protect members' benefits occurred in three major steps:

1. the introduction of the *Superannuation Industry (Supervision) Act 1993* ('*SISA*')³¹ initially with *OSSR*, and later with the *Superannuation Industry (Supervision) Regulations 1994* ('*SISR*');³²
2. the establishment of a single prudential authority, Australian Prudential Regulation Authority ('*APRA*')³³ for funds with five members or more. At the same time, funds that complied with the definition of 'self managed superannuation fund' were transferred to the Australian Taxation Office for it to act as the Regulator of these funds;³⁴
3. licensing of trustees with consequential effects.³⁵

Each of these steps resulted from reports from committees appointed by the Federal Government. The first step incorporated many of the recommendations in the Report of the Senate Select Committee on Superannuation. The second and third steps, whilst included in recommendations in the Senate Select Committee's

³⁰ Paper 2 'Occupation Superannuation Standards (OSS) Regulations Disclosure of Information to Members of Superannuation Funds'.

³¹ *Superannuation Industry (Supervision) Act 1993*, No 78 1993.

³² Commonwealth of Australia, *Superannuation Industry (Supervision) Regulations*, Statutory Rules No 57 1994, 11 March 1994.

³³ *Australian Prudential Regulatory Authority Act 1998*, No 50 1998.

³⁴ *Superannuation Legislation Amendment Act (No 3) 1999*, No 121 1999.

³⁵ *Superannuation Safety Amendment Act 2004*, No 53 2004.

Report, resulted from subsequent Reports of the Financial System Inquiry and the Superannuation Working Group.

These steps provided protection of members' benefits additional to those provided by the OSSA and OSSR to ensure the members' entitlements would be available when required, make trustees of superannuation funds accountable for their responsibilities and included provisions within the legislation to prevent abuse of the superannuation system.

For the purposes of discussion in this Chapter, discussion of the regulations of the SISA and SISR includes the amendments to the original legislation so that the evolution of the regulations to the current time is addressed.

7.2 Report to the Government – Senate Select Committee

On 5 June 1991, the Senate of the Federal Government³⁶ established a Senate Select Committee ('SSC') on Superannuation to inquire into and report on various issues relating to superannuation. This Committee issued a number of reports, the first of which was 'Safeguarding Super, The Regulation of Superannuation'.³⁷

The SSC undertook to collect as much data from as many sources as possible to ensure research on which to base its recommendations was relevant and appropriate. It received 212 written submissions and questioned numerous witnesses. It had a number of public hearings and technical briefing sessions. This approach to the inquiry provided the Committee with an

³⁶ The Australian Labor Party government under the Prime Minister Rt Hon Robert James Hawke, AC.

³⁷ Senate Select Committee, Parliament of the Commonwealth of Australia, *Safeguarding Super, the Regulation of Superannuation* (1992).

understanding of the issues within the superannuation industry and a basis for making recommendations to improve the regulatory infrastructure that governed the administration and investment of superannuation funds.³⁸

Some issues identified by previous Committees as relevant to the protection of members' benefits and included in the OSA and OSSR, were included again in the terms of reference for this inquiry:

1. constitutional arrangements governing superannuation;
2. rules applying to ... the vesting and preservation of benefits;
3. the information available to members of superannuation funds;
4. the representation of fund members in trustee structures of superannuation funds; and
5. the investment of moneys by superannuation funds.

Additional issues relevant to the protection of members' benefits and the responsibility of trustees included:

1. the adequacy of prudential control arrangements applying to superannuation funds;
2. the level and structure of fees and commissions charged in relation to superannuation fund membership and asset management;
3. the dispute resolution mechanisms available to members of superannuation funds;
4. the simplifying of superannuation.³⁹

The recommendations of the SSC were designed to make trustees more accountable to members, to provide a greater role for

³⁸ Ibid 2 [1.2]-[1.6].

³⁹ Ibid 1.

members and increase the role of the ISC in ensuring prudential standards were met. They included recommendations on:

1. the role and power of the ISC in the regulation and supervision of superannuation funds;⁴⁰
2. amendments to or replacement of provisions in the O SSA to clearly identify in the legislation:
 - (i) in-house asset rule;⁴¹
 - (ii) investment by superannuation funds;⁴²
 - (iii) trustee representation and independent public trustees;⁴³
 - (iv) the rights of members;⁴⁴
 - (v) the role of auditor;⁴⁵
3. use of fund surpluses and reserves;⁴⁶
4. imposition of penalties by ISC;⁴⁷
5. the requirements to be eligible to act as a trustee, director of a trustee company or investment manager;⁴⁸
6. the duties of trustees and directors of corporate trustees;⁴⁹
7. dispute resolution;⁵⁰
8. licensing of trustees and fund managers;⁵¹
9. reporting and disclosure;⁵²
10. fees.⁵³

⁴⁰ Ibid xv [3.1]-[3.2]; xv-xvi [4.1]-[4.3]; xvii [4.8]; 23-25 [3.1]-[3.15]; 26-27 [3.24]-[3.28].

⁴¹ Ibid xxii [7.1]-[7.2]; 85-87 [7.1]-[7.9].

⁴² Ibid xxii [9.1]-[9.4]; 101-116 [9.1]-[9.44].

⁴³ Ibid xix-xx [5.1]-[5.7]; 57-72 [5.1]-[5.39].

⁴⁴ Ibid xvii [4.9]; 44-45 [4.44].

⁴⁵ Ibid xviii [4.11]-[4.12]; 46-50 [4.47]-[4.50].

⁴⁶ Ibid xx-xxi [6.1]-[6.2]; xxi [6.4]; 73-80 [6.1]-[6.12]; 81 [6.14]-[6.15].

⁴⁷ Ibid xvii [4.7]; 43-44 [4.42].

⁴⁸ Ibid xvi [4.5]; 42 [4.37].

⁴⁹ Ibid xvi [4.4]; 41-42 [4.36].

⁵⁰ Ibid xxiv-xxv [11.1]-[11.4]; 135-143 [11.1]-[11.44].

⁵¹ Ibid xxii [8.1]-[8.2]; 89-93 [8.1]-[8.22].

⁵² Ibid xviii-xix [4.13]; xx [6.2]-[6.3]; [8.3]-[8.6]; 50-54 [4.52]; Attachment – Chapter 4.

⁵³ Senate Select Committee, Parliament of the Commonwealth of Australia, *Super – Fees, Charges and Commissions* (1993).

There were recommendations relating to marketing, competition and products that, although they provide a form of protection to members, are beyond the scope of this thesis.

The OSSA provided the mechanism for members to indentify, quantify and own their benefits. Implementation of the recommendations of the SSC would provide the additional security to members' benefits by giving members rights and making trustees responsible. It would be a further step in the evolution of the regulation of superannuation funds to protect members' benefits. The amended regulation and supervision of superannuation funds would provide a framework to further promote confidence of members in the superannuation system.

7.2.1 *The Government's Response to the SSC Report*

The recommendations by the SSC addressed the inadequacies remaining after the introduction of the OSSA and the OSSR relating to the protection of members' benefits. These outstanding issues generally involved the trustees and their accountability. Measures to be implemented were to include flexible sanctions for breaches of standards, encouragement of a diversification of investments without directing where investments were to be made, the development of a dispute resolution mechanism and the introduction of new disclosure requirements from 1 July 1992.⁵⁴ A framework and regulation to enable the implementation of these measures had to be developed.⁵⁵

⁵⁴ Treasury, Bills Digest Service, *Superannuation Industry (Supervision) Bill 1993*.

⁵⁵ The SSC reviewed the *Superannuation Industry (Supervision) Bill 1993* and other related Bills and proposed regulations. It provided comments and recommendations, some for amendment to the current Bills and regulations and some for future consideration. The Reports relevant to this thesis are:
Senate Select Committee, Parliament of the Commonwealth of Australia,
Safeguarding Super the Regulation of Superannuation (June 1992);
Super Guarantee Bills (June 1992);

7.2.2 *The role and power of the ISC*

As part of improving the framework for the supervision of the superannuation industry, as was the case when considering the introduction of the OSSA,⁵⁶ the question of the powers conferred on the Parliament by the *Constitution* was raised. In the OSSA, the Federal Government relied on the taxation power in the *Constitution* to regulate superannuation funds.⁵⁷ The OSSA provided a mechanism for superannuation entities to access concessional tax treatment by complying with operational standards.⁵⁸ This was unsatisfactory as a failure by trustees to comply with the OSSA was not an offence.⁵⁹ A federal agency was not able to prosecute the trustees unless there was non-compliance with the request to provide documents.⁶⁰ The only penalty able to be imposed for non-compliance with the OSSA was the loss of tax concessions for the superannuation fund. This cost to the superannuation fund might have been compounded if members had suffered serious financial loss as a result of the trustee's action within the superannuation fund.⁶¹ The punishment of loss of tax concessions penalised the members, who might have been victims and not the perpetrators of the breach of the legislation.⁶² Under the OSSA, there was the power to waive the penalty in the case of less serious offences, allowing them to go

Super and the Financial System (October 1992);
Super – Fiscal and Social Links (December 1992);
Super Fees, Charges and Commissions (June 1993);
Super Supervision Bills (June 1993);
Super Complaints Tribunal (October 1993);
Super Regs I (August 1994);
Super Regs II (November 1994);
Review of Superannuation Complaints Committee (April 1996).

⁵⁶ The Hancock Report 51-2 [4.19]-[4.20]; the Campbell Report 346 [20.105]; 789 [45.150]; the Task Force 30[4.4].

⁵⁷ Chapter 6 [6.2.5.2].

⁵⁸ SSC Report 24 [3.13].

⁵⁹ Ibid [3.14].

⁶⁰ *Taxation Administration Act 1953*, ss 8AA, 8C.

⁶¹ SSC Report [3.15].

⁶² Ibid 24 [3.14].

unpunished.⁶³ The members could take action against trustees to recover damages if there had been negligence or fraudulent behaviour, an expensive and sometimes questionable course of action.⁶⁴ Also, the ISC had no power to appoint administrators to preserve the assets of the fund or to take other action to protect the members' benefits.⁶⁵

The Federal Government examined how it might be able to exercise a more secure and more comprehensive degree of regulatory power over superannuation. It was part of the Terms of Reference to the Senate Select Committee.⁶⁶ On the possible use of the pension power, *Constitution* s 51(xxiii), Mr Dennis Rose QC, Chief General Counsel, Attorney-General's Department advised the Committee that:

The pensions power – the power to make laws with respect to invalid and old age pensions – would enable the Commonwealth Parliament to regulate private superannuation schemes so far as they provide for pensions for people over 60 or to people who are incapacitated, either wholly or partially.⁶⁷

Consideration was given to the power of the *Constitution* that allowed the regulation of trading or financial corporations.⁶⁸

Reliance on this power would make directors of trustee companies directly accountable to the controlling authority. This authority could instigate proceedings against them for breaches of the relevant legislation.

⁶³ Ibid 25 [3.15].

⁶⁴ Ibid 32 [4.13].

⁶⁵ Ibid.

⁶⁶ Ibid 1 [1.1(a)].

⁶⁷ Ibid 26 [3.21].

⁶⁸ *Constitution* s 51(xx).

The ISC and the Australian Law Reform Committee advocated a combination of the corporations and pensions power. Mr Rose expressed the view that:

the use of the tax power combined with the corporations power really offers the simplest, neatest scheme because there are no holes in that as there are in the pensions power.⁶⁹

Subsequently, the Attorney-General's Department advised that the Federal Government could exercise, through the ISC, an enforcement power over superannuation funds which would be based on a combination of the taxation, corporations and pensions powers of the Constitution.⁷⁰ The Federal Government proceeded in the design of the new legislation to rely on the taxation power⁷¹, corporations power⁷² and the pension power⁷³.

7.2.3 *The introduction of SISA*

In October 1992, the Treasurer announced new prudential arrangements for superannuation to protect members' benefits.⁷⁴ The introduction of the *Superannuation Industry (Supervision) Act 1993* ('SISA')⁷⁵, initially with the *OSSR* and later the introduction of the *Superannuation Industry (Supervision) Regulations 1994* ('SISR')⁷⁶, gave effect to measures to substantially increase the level of prudential protection provided to the superannuation industry. These measures represented a substantial strengthening of the security of members' benefits and protected members' rights.

⁶⁹ SSC Report 26-7 [3.26].

⁷⁰ Ibid 27 [3.27].

⁷¹ *Constitution* s 51(ii).

⁷² Ibid s 51(xx).

⁷³ Ibid s 51 (xxiii).

⁷⁴ The Treasurer, the Rt Hon John Dawkins, *Strengthening Super Security: New Prudential Arrangements for Superannuation*, (Australian Government Publishing Services, October 1992).

⁷⁵ *Superannuation Industry (Supervision) Act*, No 78 1993, Date of Assent 30 November 1993.

⁷⁶ See above n 32.

These new prudential arrangements provided:

- effective supervisory arrangements involving direct enforcement powers for the Insurance and Superannuation Commission enabling effective enforcement of the prudential requirements and obligations placed on funds and trustees;
- for trustees and investment managers to be made subject to adequate legislative sanctions for the proper performance of their fiduciary responsibilities and increasing their accountability to their members;
- clear delineation of the basic duties and responsibilities of trustees, and indicating that trustees have primary responsibility for the operation of funds;
- that trustees and investment managers must be suitable to act as fund trustees and to manage fund moneys respectively;
- for financial assistance to be provided to funds that have suffered a loss due to fraudulent conduct or theft; and
- mechanisms for dealing with benefits in employer-sponsored funds in respect of members that have left employment or who are lost, and unclaimed benefits;
- for equal member and employer representation;
- certain disclosure obligations in respect of auditors and actuaries of funds; and
- rules relating to invitations and offers to subscribe for interests in, and disclosure by, public offer superannuation funds, approved deposit funds and pooled superannuation trusts.⁷⁷

The structure of the *SISA* was well defined with the subject matter separated into parts clearly labelled as to content. The definitions and terms had clarity of language. The ATO and ASIC provided Releases and ISC/APRA provided Superannuation Circulars and Guidelines to assist in interpretation of the application of the *SISA* and *SISR*.

⁷⁷ Superannuation Industry (Supervisory) Bill 1993 Explanatory Memorandum *General outline and main purpose of the Bill*.

The principles identified and developed for the protection of members' benefits and implemented in the operating standards in the OSSA and OSSR were incorporated in the SISA. Whilst these principles were generally adopted by the SISA, there was some amendment of their application on enactment and a number of amendments were made subsequently to strengthen the provisions.

A vital component of the SISA was the inclusion of the penalty provisions with penalties identified for breaches and the ability of the Regulator to disqualify and remove the trustee and later the auditor and actuary of a superannuation entity.

7.2.4 Sole Purpose Test under SISA

The principle relating to the sole purpose for maintaining a superannuation fund provided protection for members. There were two categories of purpose, core and ancillary. The SISA incorporated details of these purposes.⁷⁸ The inclusion of this test in the SISA continued to provide a level of protection for members.⁷⁹ Non-compliance by the trustees was an offence.⁸⁰

7.2.5 Prescribed operating standards under SISA

Under the OSSA and OSSR, a superannuation entity had to comply with the operating standards prescribed by the OSSR. Compliance was required to qualify for concessional tax treatment. A breach of the operating standards might have meant that a fund was not a complying fund and might lose its tax concession for the year of income in which the breach occurred.

⁷⁸ SISA s 62; SISR regs 6.22B, 13.18.

⁷⁹ *Australian Prudential Regulation Authority v Derstepanian (with Corrigendum dated 17 August 2005)* [2005] FCA 1121.

⁸⁰ SISA s 62(2).

Under the *SISA* and *SISR*, to be a complying fund and be eligible for concessional tax treatment, the prescribed operating standards and all the provisions of the *SISA* and *SISR* had to be complied with. In addition, the *SISA* imposed penalties for breaches of the operating standards. See [7.2.7.1] on penalties.

Some of the operating standards in the *SISR* were prescribed for all regulated superannuation funds. Others applied in conjunction with the duties and obligations of trustees under the *SISA*. Others only applied to particular types of regulated superannuation funds.⁸¹

Some operating standards that were identified as protecting members' benefits were enhanced both on the enactment of the *SISA* with subsequent amendments to and insertions of provisions. Only those of significance and considered relevant to the discussion on protection of members' benefits, trustees' responsibilities and prevention of abuse of the superannuation system are discussed.

7.2.5.1 *in-house asset rule*

The principles underlying the in-house asset rules established in the *OSSA* and *OSSR* were adopted in the *SISA*⁸² but had restrictions and exceptions that were clearly defined so that minimal interpretation was required. The in-house asset rules in the *OSSR* applied to all employer-sponsored fund⁸³ whereas in the *SISA* they only applied to standard employer-sponsored funds.⁸⁴

⁸¹ Public offer superannuation funds; non-complying superannuation funds; standard employer-sponsored funds; pension funds; defined benefit superannuation funds.

⁸² *SISA* pt 8 div 1-5; *SISR* regs 13.22A-D. *Re QX971 and Australian Prudential Regulation Authority* 99 ESL 1, decision under review affirmed by AAT.

⁸³ *OSSR* reg 16A.

⁸⁴ *SISA* s 71. *SISA* s 16(2) (definition of 'standard employer-sponsor' as an employer who contributed to the fund for the benefit of a member or a member's dependants wholly or partly pursuant to an arrangement between the employer and the trustee of the fund).

The *SISA* also prohibited any schemes that would result in an artificial reduction in the market value ratio⁸⁵ of the fund's in-house assets aimed at avoiding the in-house asset rules.⁸⁶

The initial provisions of the *SISA* continued to be reliant on the *ITAA* for the definition of 'associate'.⁸⁷ This was rectified in 1999 by definitions inserted in the *SISA* that clarified the application of the in-house rules in circumstances involving associates.⁸⁸ Exclusions applied to the definitions of 'in-house asset'.⁸⁹ Transitional rules for compliance applied to arrangements established prior to the introduction of the new definition for superannuation funds.⁹⁰ This definition of 'associate' in the *SISA* minimised the use of superannuation funds' assets by preventing the indirect investment in or loans to a related party of the superannuation fund.

Non-compliance by the trustees of superannuation entities was an offence.⁹¹

7.2.5.2 *Investment by superannuation funds*

An inclusion in the covenants in the governing rules was that a trustee had to formulate and give effect to an investment strategy for the superannuation entity. The investment strategy had to have regard to the whole of the circumstances of the superannuation entity and in particular the following:

⁸⁵ *SISA* s 81, 82.

⁸⁶ *SISA* ss 71(2), (4), 85. Intention to avoid the in-house rules is integral in the application of the avoidance provisions. *VBU & APRA* 07 ESL 03, decision under review set aside; *Elliot v APRA* 04 ELS 09; *APRA v Holloway* 00 ESL 16; *APRA v Holloway* 00 ESL 9.

⁸⁷ *ITAA* s 26AAB(14).

⁸⁸ *SISA* pt 8 div 1 sub-div B, as inserted by *Superannuation Legislation Amendment Act (No 4) 1999*, No 199 1999.

⁸⁹ *SISA* s 71(1)(a)-(j).

⁹⁰ *SISA* pt 8 div 1 sub-div D. Some investments that were pre-11 August 1999 were excluded from the rules, *ITAA* ss 71A-B.

⁹¹ *SISA* s 84. See Chapter 3 [3.3.2].

- the risk involved in making, holding and realising, and the likely return from superannuation entity's investments having regard to its objectives and its expected cash flow requirements;
- the composition of the superannuation entity's investments as a whole, including the extent to which the investments were diverse or involved the superannuation entity in being exposed to risks from inadequate diversification;
- the liquidity of the superannuation entity's investments having regard to its expected cash flow requirements; and
- the ability of the superannuation entity to discharge its existing and prospective liabilities.⁹²

There was also a requirement for the trustee to formulate and give effect to a strategy for the prudential management of any reserves⁹³ of the superannuation entity, consistent with the investment strategy and its capacity to discharge its liabilities as and when they fell due.⁹⁴

These requirements in the *SISA* for compliance by the trustees of the superannuation entities further protected the members' benefits for their retirement and attempted to ensure the members' entitlements were available when required.

The implementation and disclosure of the investment strategy was developed and formed a substantial part of the requirements adopted for the licensing and product disclosure statements. See [7.4.1.1.] and [7.4.1.2.2] below.

⁹² *SISA* s 52((2)(f)); *SISR* reg 4.09.

⁹³ *SISA* s 115. The governing rules must not prohibit the superannuation entity from maintaining reserves.

⁹⁴ *SISA* s 52(2)(g). *Invensys Australian Superannuation Fund Pty Ltd v Austrac Investments Ltd* [2006] VSC 112: it was found that there was no illegal impediment for former members benefiting in distribution of surplus.

The consequence for a trustee contravening the covenants in the *SISA* for formulating and not giving effect to an investment strategy could result in a claim by members against the trustee for loss or damages rather than the fund and members being penalised by the Regulator.⁹⁵

7.2.6 *Non-complying fund status*

The *ITAA* required a superannuation fund to be a complying superannuation fund for it to be eligible for concessional taxation treatment. Prior to a fund being made non-complying, there were a number of procedures that had to occur.

7.2.6.1 *Notice of complying fund status*

The Regulator may give a notice about the complying fund status.⁹⁶ If the notice states that the fund is not a complying fund, it must state the reasons for the non-complying status.⁹⁷ It is sufficient for the Regulator to establish a contravention⁹⁸ on the balance of probabilities.⁹⁹ This allows the decision to be referred to the AAT for a review of the decision.

7.2.6.2 *Reviewable decisions*

The *SISA* and *SISR* empower the Regulator to make discretionary decisions. These decisions are called ‘reviewable decisions’.¹⁰⁰

⁹⁵ *SISA* s 55(3).

⁹⁶ *SISA* pt 5 s 40.

⁹⁷ *SISA* s 40(1), (2).

⁹⁸ *SISA* s 39(1) provides that a contravention is:

- an offence (most breaches of the *SISA* give rise to an offence);
- a contravention of a civil penalty provision; or
- a contravention of the *Taxation Administration Act 1953* (‘TAA’) Sch 1 s 288-85 (dealing with provision of false or misleading information) or div 390 (dealing with superannuation reporting).

⁹⁹ *SISA* s 39(2).

¹⁰⁰ *SISA* s 10(1), *SISR* reg 1.03(1) (definitions of ‘reviewable decision’), as inserted by Commonwealth of Australia, *Superannuation Industry (Supervision) Regulations (Amendment)*, Statutory Rules No 344, 20 December 1996.

Persons affected by such decisions have a right of review against them.¹⁰¹ The *SISA* and *SISR* set out the review procedure.¹⁰²

The affected person can request the Regulator to reconsider the decision.¹⁰³ If the person is dissatisfied with the reconsidered decision, that person make application to the AAT for a review of the decision so confirmed or varied.¹⁰⁴

By providing the opportunity for persons affected to seek a review of a reviewable decision made at the discretion of the Regulator, *SISA* and *SISR* give those persons the right to challenge the Regulator's decision at the AAT or make an application to the Regulator undertaking to rectify the contravention.¹⁰⁵

7.2.6.3 *Culpability test*

If it was found that a superannuation fund was not a complying superannuation fund, the ATO could penalise the superannuation fund (not the trustees) by not allowing tax concessional treatment.¹⁰⁶ This in turn affected the members' benefits.

One of the conditions for a complying superannuation fund to satisfy is that if the trustee breached a regulation provision in respect of the year of income on one or more occasions, the fund did not fail the culpability test.¹⁰⁷ An entity fails the culpability test if:

- (a) both:
 - (i) all of the members of the fund were in any way directly or indirectly knowingly concerned in, or party to, the

¹⁰¹ *SISA* s 344, *SISR* reg 13.26.

¹⁰² *SISA* s 344; *SISR* div 13.5.

¹⁰³ *SISA* s 344(1)-(5).

¹⁰⁴ *SISA* s 345(1); *SISR* reg 13.24(3).

¹⁰⁵ *SISA* ss 244, 262A.

¹⁰⁶ *ITAA* ss 278, 284, 285 (repealed); *ITAA* 97 s 295-25.

¹⁰⁷ *SISA* s 42(1)(b).

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- contravention, and
- (ii) APRA, after considering:
 - (A) the taxation consequences that would arise if the entity were denied concessional tax treatment in relation to the year of income concerned, and
 - (B) the seriousness of the contravention, and
 - (C) all other relevant circumstances thinks that a notice should be given stating that the fund is not a complying superannuation fund in relation to the year of income concerned, or
 - (b) all of the following conditions are satisfied:
 - (i) one or more members of the fund were in any way directly or indirectly knowingly concerned in, or party to, the contravention
 - (ii) one or more members of the fund (the ‘innocent members’) were not in any way directly or indirectly knowingly concerned in, or party to, the contravention
 - (iii) none of the innocent members would suffer any substantial financial detriment if the fund were to be taxed as a non-complying superannuation fund (ie did not receive concessional tax treatment) in relation to the year of income concerned
 - (iv) APRA, after considering:
 - (A) the taxation consequences that would arise if the fund were to be taxed as a non-complying superannuation fund in relation to the year of income concerned;
 - (B) the seriousness of the contravention, and
 - (C) all other relevant circumstances thinks that a notice should be given stating that the fund is not a complying superannuation fund in relation to the year of income concerned.¹⁰⁸

The test provides protection for the benefits of ‘innocent members’. It depends on the existence of innocent members in the

¹⁰⁸ SISA s 42(1A), inserted by *Taxation Laws Amendment Act (No 4) 1994*, No 181 1994, as amended by *Financial Sector Reform (Amendments and Transitional Provisions) Act 1998*, No 54 1998, *Superannuation Legislation Amendment Act (No 3) 1999*, No 121 1999, *Financial Services Reform (Consequential Provisions) Act 2001*, No 123 2001, *Superannuation Legislation Amendment (Simplification) Act 2007*, No 15 2007.

superannuation fund.¹⁰⁹ There must be either no ‘innocent members’ or if they do exist, they must not suffer any substantial financial detriment should the fund lose its tax concession.¹¹⁰ The question of determining this may be decided ‘on the balance of probabilities’.¹¹¹ APRA can also use its discretion to treat a non-complying fund as complying despite the culpability of fund members.¹¹²

7.2.7 Trustees

The Federal Government perceived that a framework for the prudential supervision of superannuation funds was pivotal to the protection of members’ benefits. An essential element of this framework was the role of trustees. Defining the duties of the trustees for the operation of superannuation entities was mandatory for their efficient management. The prudential authority supervising the operations of superannuation funds needed the duties defined and a mechanism to encourage and enforce their compliance.

7.2.7.1 Penalties

The *SISA* incorporated a range of penalties to provide effective enforcement of its provisions by the trustees and others responsible for the operation of superannuation funds. They were tailored to reflect the severity of any contravention.¹¹³ In all cases, a penalty could only be imposed by a court of law.¹¹⁴

¹⁰⁹ *SISA* s 42(1A)(b)(ii). *SISA* s 42A applies to self-managed superannuation funds for part year compliance.

¹¹⁰ *QX971 and APRA* 99 ESL 1.

¹¹¹ *SISA* s 42(1B).

¹¹² *SISA* s 42. *Re QX971 and Australian Prudential Regulation Authority*, 99 ELS 1, decision affirmed by AAT; *XPMX v FC of T* 08 ESL 10 [2008] AATA 981, decision set aside but with decision requiring the trustees of the Fund to provide a written undertaking to rectify the breach.

¹¹³ See above n 98.

The *Crimes Act 1914* ('*Crimes Act*') set out the general rules relating to penalties and procedures in relation to offences under Commonwealth legislation. The *Crimes Act* was replaced by the *Criminal Code Act 1995* ('*Criminal Code*').¹¹⁵ Persons accused of and prosecuted for federal offences are subject to the same principles in all parts of Australia. An offence is proved in the same way no matter where the trial is held. Chapter 2 of the *Criminal Code* (except Pt 2.5 dealing with corporate criminal liability) applies to all offences against the *SISA*.¹¹⁶ The *Criminal Code* does not of itself impose any liabilities or penalties. The penalty for a contravention of a provision of the *SISA* is a fine of the number of penalty units, or a term of imprisonment, as specified by the relevant provision breached.

Any person involved in the contravention is taken to have contravened the provision. A penalty under the *SISA* can be imposed on that person.¹¹⁷ The *SISA* and the *Criminal Code* provide statutory defences in relation to civil and criminal proceedings under the Acts.¹¹⁸ In some circumstances, the Regulator may accept enforceable undertakings by trustees to remedy problems within certain time frames as an alternative to instigating immediate enforcement action.¹¹⁹

The original *SISA* had only four categories of penalty provisions - civil penalty order, strict liability, fault liability and civil liability.¹²⁰

SISA s 39(2) provides that it is sufficient for a contravention to be established on the balance of probabilities. This allows the Administrative Appeals Tribunal ('AAT') to review a decision on a contravention.

¹¹⁴ *SISA* pt 21.

¹¹⁵ *Criminal Code Act 1995*, No 12 1995.

¹¹⁶ *SISA* s 9A, as inserted by *Treasury Legislation Amendment (Application of Criminal Code) Act (No 1) 2001*, No 31 2001.

¹¹⁷ *SISA* s 194.

¹¹⁸ *SISA* s 323, *Criminal Code Act 1995* pt 2.3.

¹¹⁹ *SISA* s 262A, as inserted by *Financial Sector Legislation Amendment Act (No 1) 2000*, No 160 2000.

¹²⁰ *SISA* pt 21; *Crimes Act 1914*.

The *SISA* now contains five categories of penalty provisions. The two-tier liability provision with a strict liability limb and a fault liability limb was introduced from 18 January 2001.¹²¹ Many of the then existing fault liability provisions were converted to two-tier liability provisions from that date.

The following table lists the penalties available under the *SISA* for the court to impose for a contravention of the *SISA* or the *SISR*. The table summarises the defined element of each breach with the required standard of proof and maximum penalty that can be imposed.

Type of provision	Element of breach	Standard of proof	Maximum penalty
Civil Penalty ('CP') - CP order - CP offence	<ul style="list-style-type: none"> serious breach serious breach; knowingly, intentionally or recklessly; and dishonestly to achieve gain or to deceive or defraud 	civil ('balance of probabilities') criminal ('beyond reasonable doubt')	<ul style="list-style-type: none"> 2,000 penalty units compensation for loss or damage five years' imprisonment compensation for loss or damage
Strict Liability ('SL')	<ul style="list-style-type: none"> breach 	criminal	<ul style="list-style-type: none"> 600 penalty units one year's imprisonment
Fault Liability ('FL')	<ul style="list-style-type: none"> breach intentionally or recklessly 	criminal	<ul style="list-style-type: none"> 600 penalty units; six month's to five years imprisonment
Two-tier Liability ('2T') - FL - SL	<ul style="list-style-type: none"> breach intentionally or recklessly breach 	criminal criminal	<ul style="list-style-type: none"> 600 penalty units; six month's to five years imprisonment 600 penalty units one year's imprisonment
Civil Liability ('CL')	<ul style="list-style-type: none"> breach 	civil	<ul style="list-style-type: none"> liability for loss or damage

Table 11: Penalties under SISA¹²²

¹²¹ *Financial Sector Legislation Amendment Act (No 1) 2000*, No 160 2000.

¹²² CCH Australia Limited, *Superannuation Law & Practice*, (1997) [1-180].

The *SISA* also provides for the suspension or removal of a trustee.¹²³

The Federal Government's introduction of penalties for imposition on trustees of superannuation funds was to make the trustees responsible for their actions. Not only were the penalties severe, there were the possibilities of having a criminal record and being prohibited from being a trustee of a superannuation entity.

7.2.7.2 *Trustee eligibility rules*

Rules about the eligibility of trustees, custodians and investment managers of superannuation entities were introduced in the *SISA*.¹²⁴ These eligibility rules have been strengthened to further protect members' benefits. A person must not intentionally be, or act as, a trustee of a superannuation entity if the person is, or knows that he or she is, a disqualified person.¹²⁵ Similarly, a person must not be, or act as, a responsible officer¹²⁶ of a body corporate if that person is, or knows that the person is a disqualified person.¹²⁷

An individual is a disqualified person if:

- (a) at any time (including a time before the commencement of this section);
 - (i) the individual was convicted of an offence against or arising out of a law of the Commonwealth, a State, a Territory or a foreign country, being an offence in respect of dishonest conduct; or

¹²³ *SISA* pt 17. See [7.5.1.1].

¹²⁴ *SISA* pt 15.

¹²⁵ *SISA* s 126K, as inserted by *Financial Sector Legislation Amendment (Review of Prudential Decisions) Act 2008*, No 25 2008. Previously *SISA* s 121(1), as repealed by *Financial Sector Legislation Amendment (Review of Prudential Decisions) Act 2008*, No 25 2008.

¹²⁶ *SISA* s 10 (definition of 'responsible officer' of a body corporate means a director, secretary or executive officer).

¹²⁷ *SISA* s 126B.

- (ii) a civil penalty order was made in relation to the person; or
- (b) the person is an insolvent under administration; or
- (c) either:
 - (i) to the extent that the Regulator is the Commissioner of Taxation – the Regulator has disqualified the individual under section 126A; or
 - (ii) to the extent that the Regulator is APRA – the Federal Court of Australia has disqualified the individual under section 126H.¹²⁸

A body corporate is a disqualified person if any of the following apply:

- (a) the body corporate knows, or has reasonable grounds to suspect, that a person who is, or is acting as, a responsible officer of the body corporate is:
 - (i) for a person who is disqualified person only because he or she was disqualified under section 126H – disqualified from being or acting as a responsible officer of the body corporate; or
 - (ii) otherwise – a disqualified person; or
- (b) a receiver, or a receiver and manager, has been appointed in respect of property beneficially owned by the body; or
- (c) an administrator has been appointed in respect of the body; or
- (d) a provisional liquidator has been appointed in respect of the body; or
- (e) the body has been wound up.¹²⁹

The Regulator may waive the person's status as a disqualified person.¹³⁰

¹²⁸ SISA s 120, as amended by *Financial Sector Legislation Amendment (Review of Prudential Decisions) Act 2008*, No 25 2008; as amended by *Financial Sector Legislation Amendment Act (No 1) 2000*, No 160 2000.

¹²⁹ SISA s 120(2), as amended by *Financial Sector Legislation Amendment (Review of Prudential Decisions) Act 2008*, No 25 2008, *Statute Law Revision Act 2007*, No 8 2007, *Superannuation Industry (Supervision) Legislation Amendment Act 1995*, No 144 1995.

¹³⁰ SISA s 126B, as amended by *Superannuation Industry (Supervision) Legislation Amendment Act 1995*, No 144 1995, as amended by *Financial Sector Reform (Amendments and transitional Provisions) Act 1998*, No 54 1998, *Financial Sector Legislation Amendment Act (No 1) 2000*, No 160 2000. *N/2000 v APRA 02 ELS 01*

A person must provide written consent to act as a trustee of a superannuation fund, or as a director of a corporate trustee of a superannuation fund.¹³¹ This acknowledges the person's acceptance of the responsibility of the role.

The rules relating to who may be a trustee provide structural integrity to superannuation entities. This added to the mechanisms implemented to further protect members' benefits.

7.2.7.3 Duties

The trustee had to act in accordance with the trust deed. The trust deed was to include the covenants specified in the *SISA*.¹³² The duties of trustees were outlined. They included the duty to:

- establish arrangements for dealing with inquiries or complaints;¹³³
- seek information from investment manager;¹³⁴
- keep minutes and records;¹³⁵
- keep records of changes of trustees;¹³⁶
- keep reports;¹³⁷
- notify Commissioner of significant adverse events;¹³⁸
- establish procedure for appointing members representatives if the superannuation fund was an employer-sponsored fund;¹³⁹
- establish a procedure for appointing independent trustee or independent member of board of directors of corporate

[2001] AATA 979, decision under review affirmed by AAT, disqualified status confirmed.

¹³¹ *SISA* s 118.

¹³² *SISA* pt 6.

¹³³ *SISA* s 101.

¹³⁴ *SISA* s 102.

¹³⁵ *SISA* s 103.

¹³⁶ *SISA* s 104.

¹³⁷ *SISA* s 105.

¹³⁸ *SISA* s 106.

¹³⁹ *SISA* s 107.

trustee if the superannuation fund was an employer-sponsored fund;¹⁴⁰

- make investments on an arm's length basis.¹⁴¹

The 'benefit protection standards' were introduced to protect the members' benefits.¹⁴² The trustee had to determine the cost to be charged against members' benefits and the 'fair and reasonable' distribution of these costs.¹⁴³ These standards also included the determination of the allocations of investment returns to the members' benefits taking the return on investment, costs to be charged and the level of reserves.¹⁴⁴

The *SISA* made the trustee generally responsible for all operations of the superannuation entity. This made them responsible for the protection of members' benefits.

7.3 Report to the Government - Financial System Inquiry

The Federal Government¹⁴⁵ established the Financial System Inquiry in June 1996 to review the Australian financial system and recommend possible improvements to the regulatory arrangements to ensure an 'efficient, responsive, competitive and flexible financial system to underpin stronger economic performance, consistent with financial stability, prudence integrity and fairness'.¹⁴⁶ The Final Report, known as the 'Wallis Report', was delivered to the Treasurer on 18 March 1997.¹⁴⁷ Like the SSC, the Inquiry sought

¹⁴⁰ *SISA* s 108.

¹⁴¹ *SISA* s 109.

¹⁴² *SISR* pt 5.

¹⁴³ *SISR* regs 5.02, 5.02A.

¹⁴⁴ *SISR* reg 5.03.

¹⁴⁵ The Liberal-Country Party coalition government under Prime Minister the Rt Hon John Winston Howard.

¹⁴⁶ The Treasurer, the Hon Peter Costello MP, 'Financial System Inquiry: terms of reference and membership', (Press Release, 19 May 1996).

¹⁴⁷ Financial System Inquiry. Commonwealth of Australia, *Financial System Inquiry Final Report* (1997), ('Wallis Report').

wide public and finance industry participation.¹⁴⁸ Its recommendations sought to:

- create a flexible regulatory structure which will be more responsive to the forces for change operating on the financial system;
- clarify regulatory goals;
- increase the accountability of the agencies charged with meeting those goals;
- ensure that regulation of similar financial products is more consistent and promotes competition by improving comparability;
- introduce greater competitive neutrality across the financial system;
- establish more contestable, efficient, and fair financial markets resulting in reduced costs to consumers;
- provide more effective regulation for financial conglomerates which will also facilitate competition and efficiency; and
- facilitate the international competitiveness of the Australian financial system.¹⁴⁹

The Inquiry cited the higher demand for financial services arising from the demographic and life cycle changes as need for change. These included the ageing of the population and increasing expectations of higher retirement incomes and greater job mobility.¹⁵⁰

The Inquiry recommended the establishment by statute of a single body to conduct a consistent and comprehensive disclosure regime for the whole financial system. This regulator should have the responsibility for the regulation of advice and sales of retail financial products and the licensing of financial advisers. It should oversee industry based complaints and dispute resolution schemes.¹⁵¹ The new regulatory entity, the Australian Prudential Regulation Commission ('APRC') should undertake the prudential

¹⁴⁸ Ibid viii.

¹⁴⁹ Ibid 2.

¹⁵⁰ Ibid 3.

¹⁵¹ Ibid 17-21.

regulation within the financial system, combining the existing prudential regulation functions of the Reserve Bank of Australia ('RBA'), the Financial Institutions Scheme and the ISC. All prudentially regulated financial corporations were to be brought under the Commonwealth jurisdiction. The Inquiry considered that the APRC should be empowered under legislation to:

- establish and enforce prudential regulation of any licensed or approved financial entity (unlicensed entities generally would be prohibited from offering products of specified classes including deposits, insurance and retirement savings or income products);
- issue or revoke authorities for [Deposit Taking Institutions], including banks, building societies and credit unions, life and general insurance companies and friendly societies, and approvals for superannuation funds;
- administer and enforce retirement incomes policy requirements on superannuation products (other than excluded funds where the trustees are the only beneficiaries – these should be regulated by the Australian Taxation Office); and
- assume management control of any licensed financial entity that fails or is considered likely to fail under clearly defined provisions and procedures for early resolution.¹⁵²

The Wallis Report stated that prudential regulation of superannuation, where it is required, should be linked with regulation to ensure compliance with government retirement income policies, ensuring that superannuation providers face a single regulator and that inspections could be undertaken on a comprehensive basis.¹⁵³ The regulatory approach should focus on compliance issues and ensure appropriate risk management

¹⁵² Ibid 21.

¹⁵³ Ibid 332-333 [8.4.1].

practices.¹⁵⁴ It should provide market integrity and consumer protection.¹⁵⁵

The Wallis Inquiry recognised the position of superannuation funds with fewer than five beneficiaries, ‘excluded funds’. They confirmed these superannuation funds provided cost-effective superannuation vehicles for the self-employed and small businesses. The close relationship between trustees and members made it impracticable to apply prudential regulation. It suggested that the ATO should regain responsibility of self managed funds on the basis that it had the resources and powers appropriate for regulation of the taxation provisions as they applied to superannuation funds. To improve the prudential behaviour, these measures should be adopted:

- increasing the responsibilities on trustees and auditors to ensure compliance by excluded funds with retirement income laws; and
- requiring all members of excluded funds to be trustees.¹⁵⁶

7.3.1 The Government’s Response to the Wallis Report

The Federal Government adopted the recommendation for the establishment of a single regulatory body, the Australian Prudential Regulation Authority (‘APRA’), made by the Wallis Inquiry. It also adopted the recommendation that ‘excluded funds’ should not be subjected to the prudential regulations of APRA.¹⁵⁷ The regulation and supervision of these funds were transferred to the ATO. They were renamed ‘self managed superannuation funds’.¹⁵⁸

¹⁵⁴ Ibid [8.3.2] 305.

¹⁵⁵ Ibid 28, 246-8.

¹⁵⁶ Ibid [8.4.1] 333-334.

¹⁵⁷ SISA s 18A, as repealed by *Superannuation Legislation Amendment Act (No 3) 1999* No 121 1999.

¹⁵⁸ SISA s 17A, as inserted by *Superannuation Legislation Amendment Act (No 3) 1999* No 121 1999.

7.3.1.1 Introduction of APRA

The Federal Government established the Australian Prudential Regulation Authority in July 1998.¹⁵⁹ APRA was established to take responsibility for the supervision of banks, life and general insurance companies and superannuation entities. Amendments were made to the *SISA* to effect the changes necessary to implement its authority in relation to the prudential regulation of superannuation entities.¹⁶⁰ Initially, APRA replaced ISC and administered those parts of the *SISA* that ISC was responsible for.

7.3.1.2 Self managed superannuation funds

The Federal Government established the new structure for self managed superannuation funds in October 1999.¹⁶¹ The definition of ‘self managed superannuation fund’ replaced the definition of an ‘excluded superannuation fund’.

A self managed superannuation fund has fewer than five members.¹⁶² The new definition required that each trustee¹⁶³ be a member of the fund¹⁶⁴ and that each member of the fund be a trustee.¹⁶⁵ No member may be employed by another member of the fund, unless they are related.¹⁶⁶ Trustees cannot be remunerated for their duties.¹⁶⁷ The Federal Government considered that by adopting this structure, members of self managed superannuation funds would be able to protect their own interests and these funds

¹⁵⁹ *Australian Prudential Regulatory Authority Act 1998*, No 50 1998.

¹⁶⁰ *Financial Sector Reform (Amendments and Transitional Provisions) Act 1998*, No 54 1998, later amended by *Financial Sector Reform (Amendments and Transitional Provisions Act, (No 1) 1999* No 44 1999; by *Financial Sector Reform (Amendments and Transitional Provisions) Act (No 1), 2000* No 24 2000.

¹⁶¹ *SISA* s 17A, as inserted by *Superannuation Legislation Amendment Act (No 3) 1999*, No 121 1999.

¹⁶² *SISA* s 17A(1)(a).

¹⁶³ If the trustee is a body corporate, each director of the body corporate. *SISA* s 17A(1)(c).

¹⁶⁴ *SISA* s 17A(1)(d).

¹⁶⁵ *SISA* s 17A(1)(b).

¹⁶⁶ *SISA* s 17A(1)(e).

¹⁶⁷ *SISA* s 17(1)(f).

were subjected to a less onerous prudential regime under SISA.¹⁶⁸ From 1 July 2007, trustees of self managed superannuation funds had to declare that they understood their duties within 21 days of becoming a trustee or director.¹⁶⁹

The non-prudential regulation of self managed superannuation funds transferred to the ATO from 1 July 1999 while the regulation of all other funds remained with APRA.¹⁷⁰ The ATO has the responsibility of ensuring that self managed superannuation funds comply with the non-prudential requirements of SISA.¹⁷¹

Self managed superannuation funds must comply with the provisions of the *SISA* with some modifications and exemptions. The reporting to the Regulator ie the ATO¹⁷² and auditing reporting requirements¹⁷³, have different standards than those of superannuation entities regulated by APRA. The disclosure requirements do not apply to self managed superannuation funds.¹⁷⁴ The trustee of a self managed superannuation fund is not required to be registered or licensed by APRA¹⁷⁵ or to hold an Australian Financial Services Licence.¹⁷⁶ The members of a self

¹⁶⁸ Senator Vanstone Minister for Justice and Customs, 'Superannuation Legislation Amendment Bill (No 3) 1999' (Second Reading Speech at the House of Representatives, Canberra).

¹⁶⁹ *SISA* s 104A, as inserted by *Superannuation Legislation Amendment (Simplification) Act 2007*, No 15 of 2007.

¹⁷⁰ *SISA* s 252G(6). *Superannuation Legislation Amendment Act (No 3) 1999*, No 121 1999.

¹⁷¹ *SISA* 106A.

¹⁷² *SISA* s 35D (previously imposed under by *SISA* s 36A), as amended by *Financial Sector Legislation Amendment (Simplifying Regulation and Review) Act 2007*, No 154 2007); *SISR* reg 8.03; *SISA* s 36; *SISR* reg 11.02.

¹⁷³ See [7.4.1.2.1].

¹⁷⁴ See [7.4.1.2.2.].

¹⁷⁵ *SISA* s 10(1) (definition of 'registrable superannuation entity' excludes self managed superannuation fund).

¹⁷⁶ *Corporations Act* s 911A(2)(j).

managed superannuation fund do not have access to the Complaints Tribunal.¹⁷⁷

If a superannuation fund ceases to comply with the requirements that apply to a self managed superannuation fund, it does not cease to be a self managed superannuation fund until the earlier of the trustees appointing an RSE licensee¹⁷⁸ or six months have passed¹⁷⁹. If the number of members is five or greater, the fund ceases to be a self managed superannuation fund and the ATO must be notified within 21 days.¹⁸⁰

Whilst members of self managed superannuation funds should be able to protect their own interests, the lack of personal financial skills puts their benefits at risk. By having to rely on financial planners who may not act in the best interest of the members and may induce them to invest in unsuitable products and schemes, the members' benefits are vulnerable to dissipation. The licensing of financial planners with the compliance requirements attempted to overcome this.¹⁸¹ However, the regulation for self managed superannuation funds with the potential of non-compliance status of the fund¹⁸² and the potential application of penalties make the trustees¹⁸³ responsible for their actions.

7.4 Report to the Government – Superannuation Working Group

The Federal Government confirmed its policy to address the long term consequences of an ageing population.¹⁸⁴ Following some high

¹⁷⁷ See Resolution of Complaints [7.6.1].

¹⁷⁸ *SISA* s 17(4)(a).

¹⁷⁹ *SISA* s 17(4)(b).

¹⁸⁰ *SISA* s 106A.

¹⁸¹ CA pt 7.6 – licensing of providers of financial services.

¹⁸² *SISA* pt 5 div 2-3.

¹⁸³ See [7.2.7.1].

¹⁸⁴ See below n 187, Introduction.

profile cases,¹⁸⁵ it considered that it was imperative that the community had full confidence that the regulatory framework was strong and robust. It released an initial Issues Paper, *Options for Improving the Safety of Superannuation* on 2 October 2001.¹⁸⁶ This paper addressed two key issues:

- updating the prudential and legislative framework; and
- fund governance including trustee accountability to fund members.

The Federal Government established a Superannuation Working Group ('SWG') to consult on the Issues Paper. The SWG released a background paper on 24 December 2001. The final report was provided to the Federal Government on 28 March 2002.¹⁸⁷

The SWG took the view that whilst many areas of the regulatory framework were operating effectively, 'preventative maintenance' should be considered. There was a 'need for vigilance by policy makers and regulators to ensure that the regulatory framework is operating effectively, and that the regulator is appropriately resourced and able to deal with issues at an early stage.'¹⁸⁸ SWG recommended a universal licensing regime. Trustees of superannuation entities, other than self managed superannuation funds and exempt public sector superannuation schemes should be required to:

- comply with conditions on a licence, with other legislative requirements and with covenants in the trust deed;

¹⁸⁵ Collapse of the HIH Insurance Group. APRA Media releases and reports released by SSC: the Corrections Corporation Staff Superannuation Fund, the Media Labs Superannuation Fund, the Hairdressers Association Superannuation Fund, Employees Productivity Award Superannuation Fund, the Law Employees Superannuation Fund.

¹⁸⁶ The Minister for Financial Services & Regulation, the Hon Joe Hockey MP, Liberal-Coalition Party under the Prime Minister, the Hon John Winston Howard.

¹⁸⁷ Superannuation Working Group, Commonwealth of Australia, *Report of the Superannuation Working Group on Options for Improving the Safety of Superannuation* (2002).

¹⁸⁸ Superannuation Working Group, Commonwealth of Australia, *Options for Improving the Safety of Superannuation* (2002) 11.

- have adequate resources in place (financial ..., technological and human resources);
- meet minimum standards of competency;
- have adequate risk management systems in place, including a risk management plan and adequate arrangements for ensuring compliance with the plan;
- have adequate levels of professional indemnity insurance and material damage/consequential loss insurance in place; and
- meet any other conditions as prescribed in regulations or as required by APRA.

Licensees would also need to meet these licence criteria on an on-going basis.¹⁸⁹

There were twenty eight recommendations. Of these, a number related to the protection of members' benefits and were instrumental in the licensing and registration process. They included:

- risk management plans;
- prudential standards for capital, investment rules, outsourcing, governance and operational risk;
- capital adequacy;
- registration of funds.¹⁹⁰

7.4.1 The Government's Response to the SWG Report

The Federal Governments adopted a number of the SWG's recommendations.¹⁹¹ It introduced, inter alia, a universal licensing regime requiring trustees of superannuation entities regulated by APRA to be licensed and registration of those entities.¹⁹² This improved the standard of those in the responsible position of trustee of superannuation entities.

¹⁸⁹ Ibid 1.

¹⁹⁰ Ibid 1-8.

¹⁹¹ Minister for Revenue and Assistant Treasurer, Senator Coonan, 'Superannuation Safety Amendment Bill 2003', (Second Reading Speech delivered at the Senate in Parliament House, Canberra, 9 March 2004).

¹⁹² *Superannuation Safety Amendment Act 2004*, No 53 2004.

Although the provisions of *SISA* and the regulation of *SISR* have been only minimally changed since their insertion in 2004, APRA developed its own guidelines for the implementation of the licensing and registration.¹⁹³

7.4.1.1 *Licensing trustees*

Before 1 July 2004, trustees of public offer entities had to be approved by APRA. These funds had to have an ‘approved trustee’ before they were allowed to operate.¹⁹⁴

From 1 July 2004, corporate trustees and groups of individual trustees of certain APRA regulated superannuation entities were required to be licensed by APRA.¹⁹⁵ The trustee of a public offer fund had to be a constitutional corporation.¹⁹⁶ Registrable superannuation entities (‘RSE’) were to be registered with APRA, in accordance with *SISA*.¹⁹⁷

A RSE meant a regulated superannuation fund, an ADF or a PST, but not a self managed superannuation fund.¹⁹⁸ An RSE included a public offer superannuation fund, a small APRA fund¹⁹⁹ or an eligible rollover fund.

APRA administers trustee licensing and RSE registration under the *SISA*.²⁰⁰ Licensing of superannuation trustees ensures that they

¹⁹³ The Auditor-General, ‘APRA’s Prudential Supervisions of Superannuation Entities’, Audit Report No 6 2003-04 Performance Audit.

¹⁹⁴ *SISA* pt 2, as repealed by *Superannuation Safety Amendment Act 2004*, No 53 2004 effective from 1 July 2006.

¹⁹⁵ *SISA* pt 2A; *SISR* reg 3A pt 3A, as inserted by *Superannuation Industry (Supervision) Regulations (Amendment)* Statutory Rule No 113 2004.

¹⁹⁶ *SISA* s 29C.

¹⁹⁷ *SISA* pt 2B.

¹⁹⁸ *SISA* s 10(1) (definition of ‘registrable superannuation entity’).

¹⁹⁹ A small APRA fund is a superannuation fund with less than 5 members that does not satisfy the conditions to qualify as a self managed superannuation fund and which has an RSE licensee appointed as its trustee.

²⁰⁰ *SISA* pt 2A divs 4-7.

comply with certain standards of probity and competence. Conditions for being granted and holding a RSE licence include the requirement for trustees to meet minimum standards of fitness and propriety.²⁰¹ An application for a licence must have an appropriate risk management plan and outsourcing arrangements to look after the interests of members.²⁰² The applicant must have sufficient resources, both financial and human. Licensees must maintain risk management strategies covering the licensee's operations and risk management plans for each fund under the licensee's control.²⁰³ The trustees must address the possibility of having a conflict of interest and provide a plan to deal with such an event.²⁰⁴ APRA may impose additional conditions on licences or issue directions to licensees. This enables APRA to respond to specific prudential issues before they could become actual risks to members' benefits.²⁰⁵

The registration of RSEs, among other things, provides a mechanism by which APRA can obtain information about superannuation entities that it regulates.

The trustee of a RSE has to provide APRA information to assist members of the public to identify registered RSEs and their RSE licensees, as well as provide the contact details of the RSEs and their RSE licensees.²⁰⁶ APRA is required to maintain a public

²⁰¹ *SISA* s 29D(1)(d).

²⁰² *SISA* s 29E(1)(c). An application for an APRA licence is comprehensive in the information that is required. The interpretation of the requirements under the *SISA* are provided by APRA: APRA Superannuation Guidance Notes SGN 110.1 (Fit and Proper); SGN 120.1 (Risk Management); SGN 130.1 (Outsourcing); SGN 140.1 (Adequacy of Resources); SGN 150.1 (Capital Requirements – Net Tangible Assets).

²⁰³ *SISA* s 29E(1)(c).

²⁰⁴ ASIC Policy Statement 181 Licensing: Managing Conflict of Interest.

²⁰⁵ *SISA* s 29EA.

²⁰⁶ *SISA* s 254; *SISR* pt 11.

register of this specified information and make it available to the public.²⁰⁷

It is an offence for a person to be the trustee of a RSE unless the person is a body corporate or a member of a group that hold a RSE licence from 1 July 2004. In the case of trustees existing on 1 July 2004, this applied from 1 July 2006.²⁰⁸

In summary:

- all trustees operating an APRA regulated superannuation entity must hold an RSE licence. Trustees of self managed superannuation funds or public sector superannuation schemes are excluded;²⁰⁹
- an 'RSE licence' means a licence granted by APRA²¹⁰. A 'RSE licensee' means a constitutional corporation, body corporate or group of individual trustees which holds an RSE licence granted under that section;
- all superannuation entities, other than self managed superannuation funds and exempt public sector superannuation schemes, must be registered with APRA.²¹¹ Only an RSE licensee can register a superannuation entity;²¹²
- to qualify for an RSE licence, the trustee or group of individual trustees must have a risk management strategy²¹³ and satisfy various standards as prescribed by the *SISR*;²¹⁴ and

²⁰⁷ *SISR* pt 11A.

²⁰⁸ *SISA* s 29J.

²⁰⁹ *Financial Sector (Collection of Data) Act 2001* s 7.

²¹⁰ *SISA* s 29D.

²¹¹ *SISA* ss 29K, 29E(1)(d).

²¹² *SISA* ss 29L.

²¹³ *SISA* s 29P.

²¹⁴ *SISA* pt 2A, div 8.

- to register a fund or trust, the trustee or group of individual trustees must have a risk management plan for that fund or trust.²¹⁵

The requirements for licensing of trustees imposed by the *SISA* protect members' benefits by limiting those who can be a trustee and issue superannuation interests²¹⁶ in non-public offer and public offer entities.²¹⁷ APRA has the ultimate power of licensing trustees and, by this process, confirming their appointment.

7.4.1.2 *Consequences of licensing and registration.*

As a result of the licensing and registration provisions of the *SISA*, there were consequences that increased the protection of members' benefits and made trustees more accountable for their responsibilities. The *Corporations Act 2001* ('CA') applied to the issue of interests in a superannuation entity.²¹⁸ The reporting, accounting and auditing provisions of the CA applied to superannuation entities, except self managed superannuation funds. This application of the CA to RSEs meant that the ASIC became involved in the regulation of superannuation entities.²¹⁹ Whilst it involved another authority in the regulation, it removed the duplication of supervision and regulatory activities.²²⁰ The

²¹⁵ *SISA* s 29L(2)(e).

²¹⁶ *SISA* s 10(1) (definition of 'superannuation interest' means a beneficial interest in a superannuation entity').

²¹⁷ *SISA* s 152; *FSCDA* s 13.

SISA s 10(1) (definition of 'public offer entity' means:

(a) a public superannuation fund; or
 (b) an approved deposit fund that is not an excluded approved deposit fund; or
 (c) a pooled superannuation trust.)

SISA s 18 defines 'public offer fund'.

²¹⁸ *SISA* s 38A(b) (definition of 'regulatory provision'); *Corporations Act 2001* pt 7.9, as amended by the *Financial Services Reform Act 2001*.

²¹⁹ The Corporate Law Economic Reform Program (CLERP) was initiated in 1997 as a vehicle for the ongoing review and reform of Australia's corporate and business regulation to ensure that it is modern, responsive and promotes business activity. The reforms implemented by this program now applied to RSEs.

²²⁰ CA s 5B.

corporate trustees' responsibility to comply with the CA continued to apply to them.

7.4.1.2.1 Accounts and auditing

A trustee is required to:

- keep and retain accounting records;²²¹
- prepare reporting documents or accounts and statements;²²²
- appoint an auditor to audit the superannuation entity's accounts and statements and receive an audit report from the auditors;²²³
- give a copy of the audit report to APRA.²²⁴

The provisions of the *SISA* and the *SISR* as originally enacted were amended to improve the trustee's obligations for the accounts, audit and reporting.²²⁵ The penalties imposed for not keeping accurate records remained in the *SISA*²²⁶ with the imposition of penalties for intending to deceive, mislead or provide false or misleading information being transferred to the CA.²²⁷ Failure by the trustee to arrange an audit or respond to a request from the auditor for documents was an offence.²²⁸

All registered schemes must comply with the accounting and auditing provisions of the CA.²²⁹ This statutory duty applied to

²²¹ *SISA* s 35A(2) (previously imposed by *SISA* s 111(2)).

²²² *SISA* s 35A (previously imposed by *SISA* s 111; *FSCDA* s 13; *SISR* pt 9).

²²³ *SISA* s 35C (previously imposed by *SISA* s 113); *FSCDA* s 13.

²²⁴ *SISA* s 36 (applicable only to RSEs).

²²⁵ *SISA* pt 13, as repealed by, *SISA* pt 4, as inserted by *Financial Sector Legislation Amendment (Simplifying Regulation and Review) Act 2007*, No 154 2007; *SISR* reg 8.01-8.14, as amended by SLI No 343 2007.

²²⁶ *SISA* pt 26.

²²⁷ CA pt 7.9 div 7.

²²⁸ *SISA* s 113(2), (2A).

²²⁹ CA pt 2M.3.

financial years starting on or after 1 July 2004 to coincide with the licensing provisions.²³⁰

Audits for the purposes of the *SISA* are carried out in accordance with the Australian Auditing Standards issued by the Auditing and Assurance Standards Board ('AUASB').²³¹

To be eligible to audit the financial statements of superannuation funds, an auditor has to be an 'approved auditor'.²³² The rules about the obligations and penalties for auditors in relation to superannuation entities were included in the *SISA*.²³³

The audit process provides a mechanism to review the records of a RSE and check the accuracy of those records. The requirement for auditors to qualify the reports and report prescribed breaches of the *SISA* to the Regulator adds to the level of protection for members' benefits.²³⁴

7.4.1.2.2 Reporting

The trustee of a registered scheme must comply with the requirements for providing information to new and existing members of a superannuation entity as set out in the *CA*.²³⁵

²³⁰ *Superannuation Safety Amendment Act 2004*, No 53 2004.

²³¹ *CA* ss 307A, 336.

The AUASB is a Commonwealth statutory body charged with the responsibility of issuing statutory auditing standards. New standards were issued in 2006 that conform to International Standards on Auditing issued by the International Auditing and Assurance Standards Board.

²³² *CA* pt 9.2; *SISA* s 10(1) (definition of 'approved auditor'); *SISR* Schedule 1AAA, as inserted by Commonwealth of Australia, *Superannuation Industry (Supervision) Regulations (Amendment)*, Statutory Rules No 430, 22 December 1995. There is no requirement for auditors to be independent for any class of superannuation entity as was required under *OSSA*.

²³³ *SISA* pt 16.

²³⁴ *SISA* s 129(3).

²³⁵ *CA* pt 7.9.

1. Product Disclosure Statement

The financial product disclosure requirements and other provisions relating to the issue or sale of financial products²³⁶ are set out in the CA.²³⁷

2. Periodic reporting

The content of a periodic statement to members must include:

- information relating to the management, financial condition and investment performance of the entity;
- information that a member could reasonably be expected to need to understand his or her investment in the financial product. Specific contents must be contained in the statement.²³⁸

Disclosure of details of fees, charges or expenses must be included in the periodic statement.²³⁹

On the basis that members of self managed superannuation funds are able to protect their own interests and the trustees are not required to be licensed, they are not subject to reporting and requirements under the CA.²⁴⁰

The requirements for disclosure and reporting make the trustee responsible for the information on which members make their decisions. On the basis that the information is accurate and all

²³⁶ CA s 764A(g) includes a superannuation interest, as defined by the *SISA*, as a financial product.

²³⁷ CA pt 7.9 div 2 sub-div A-F; CR pt 7.9 div 2.
ASIC has issued Regulatory Guide RG 168 *Disclosure: Product Statements (and other disclosure obligations)*. This includes the Good Disclosure Principles.

²³⁸ CA ss 1017D, 1017DA; *Corporations Regulations 2001* Ch 7 pt 7.9.

²³⁹ CA s 1017D; CR reg 7.9.20A, inserted by Commonwealth of Australia, *Corporations Amendment Regulations* Statutory, Rules 2004 No 149. 24 June 2004.

²⁴⁰ *SISA* s 35B, (previously imposed by *SISA* s 112).

information is provided, it also makes members responsible for their decisions.

7.4.1.3 Monitoring by APRA

APRA's role increased with the introduction of the licensing²⁴¹ and registration²⁴² provisions of the *SISA*²⁴³ and the collection of data for analysis and reporting to the Federal Government.²⁴⁴

With this increased role, APRA developed its prudential overview process (called 'review', not audit) to implement its functions under the *SISA*.²⁴⁵ APRA's power within the *SISA* to audit superannuation entities includes a review not only of their past compliance but also of their controls and operations to prevent future breaches. This process ensures that the trustees are performing their duties and protecting members' benefits. The objectives in conducting reviews are to ensure that:

- the assets of the fund are secure to finance the members' benefits;
- the trustees are making decisions about the operation of the fund and these decisions are implemented;
- the members are kept informed about their benefits and the fund;
- superannuation funds are managed prudently and diligently;
- trustees are aware of and carry out their duties in accordance with the deed and legislation.²⁴⁶

Whilst the selection of a trustee to be reviewed is based on APRA's policy to review funds every few years, some superannuation

²⁴¹ *SISA* pt 2A.

²⁴² *SISA* pt 2B.

²⁴³ *Superannuation Safety Amendment Act 2004*, No 53 2004.

²⁴⁴ *Financial Sector (Collection of Data) Act 2001*, No 121 2001.

²⁴⁵ *SISA* pt 25 div 2.

²⁴⁶ Thomson Reuters (Professional) Australia Limited, *Superannuation Practice Manual for APRA Compliance*, vol 1 (at April 2010) 1001-2 [6-0000]-[6-0030].

entities have been selected for audit because APRA or ASIC has received allegations or complaints against the fund or because the Superannuation Complaints Tribunal requests a review.²⁴⁷ APRA has also reviewed audit procedures adopted by major audit firms which have substantial superannuation entities as clients.²⁴⁸

As part of the initial licensing process and the ongoing review process, APRA looks at five key aspects of a superannuation entity:

- a control and compliance regime which effectively addresses the trustee's legislative obligations and other identified fund risks. This regime includes the decision making and implementation process and monitoring and recording decisions;
- a risk assessment process which identifies all risks and emerging challenges both in terms of internal decision, control processes and the external environment. The process includes the implementation, internal review and remedial action if required;
- an investment strategy which is consistent with, and is being implemented to achieve, the investment objective adopted for the fund;
- management with high standards of competence, integrity and knowledge to properly carry out its responsibilities to members of the fund and, where appropriate, implement corporate governance initiatives such as a 'conflict of interest' policy and a policy in relation to related party transactions and disclosure.
- a strategic plan that places due focus on the long-term nature of the members' interests.²⁴⁹

²⁴⁷ Ibid 1002 [6-0035].

²⁴⁸ Ibid.

²⁴⁹ Ibid 1004-5 [6-0050].

As part of the its review process, APRA checks the following and ensures compliance with the *SISA* for protection of members' benefits:

- governing rules, including that the fund complies with the sole purpose test;
- benefits and contributions, including allocation and preservation of members' benefits;
- investments;
- asset verification;
- investment strategy;
- derivatives risk statement;
- acquisition and disposal;
- borrowings;
- member reporting (generally done by ASIC);
- trustee responsibilities, including equal representation rules and procedures for handling member enquiries and complaints;
- insurance policies;
- administrative systems and controls, including monitoring of service providers and implementation of control systems;
- actuary, including confirmation of actuarial investigation and current funding and solvency certificate.²⁵⁰

The pro-active role of APRA in its reviews of superannuation entities provides a mechanism for the protection of members' benefits by ensuring trustees implement the strategies and plans provided to APRA as an indication of their competency and good intentions. Combined with role of ASIC, the supervision of the trustees and the records and reporting has been developed to a high standard.

²⁵⁰ Ibid 1013-17 [6-0070]-[6-0160].

7.5 Remedies available for protection

Trustees are responsible for the operation of a superannuation entity. Auditors are responsible for ensuring that the trustees are recording the transactions carried out by the trustee accurately and that the trustees are complying with the requirements of the *SISA* and *SISR*. If either the trustees or auditors are not performing the duties as prescribed by the *SISA*, the Regulator can impose penalties and sanctions prescribed by the *SISA* on trustees²⁵¹ and auditors.²⁵² In addition, the Regulator has the power under the *SISA* to remove them from their position. It is the Regulator who has the ultimate power to protect the members' benefits and make the trustees responsible.

7.5.1 The Regulator

7.5.1.1 The trustees

The Regulator has the authority under the *SISA* to suspend or remove the trustee of a superannuation entity in certain circumstances.²⁵³ If the Regulator takes this action, an acting trustee must be appointed.²⁵⁴

The Regulator may disqualify an individual or an individual who is or was a responsible officer of a trustee, investment manager or custodian (the body corporate) if:

- the individual or the body corporate has contravened the *SISA* or the *Financial Sector (Collection of Data) Act 2001* ('*FSCDA*') on one or more occasions; and

²⁵¹ See [7.5.1.1].

²⁵² See [7.5.1.2].

²⁵³ *SISA* s 133. 06 ESL 11, the AAT confirmed the decision of APRA to disqualify the applicant as trustee under *SISA* s 133(1), period of disqualification was for two years, *VBU & APRA* 07 ESL 03, decision under review set aside.

²⁵⁴ *SISA* s 134.

- the nature or seriousness of the contraventions(s), or the number of contraventions, provides grounds for disqualification.²⁵⁵

The Regulator may disqualify a person if not satisfied that the individual is a ‘fit and proper person’.²⁵⁶

The disqualification may be revoked on application by the disqualified individual or by the Regulator²⁵⁷. The Regulator must give written notice of any disqualification, revocation of a disqualification or a refusal to revoke disqualification.²⁵⁸

The Regulator may apply to the Federal Court to disqualify a person from being or acting as a trustee of a superannuation entity (not a self managed superannuation fund) or a responsible officer of a body corporate that is a trustee, or an investment manager or custodian of a superannuation entity (other than a self managed superannuation fund)²⁵⁹ for committing offences.²⁶⁰ The grounds for the application to the Federal Court for disqualification are

²⁵⁵ SISA s 126A(1), (2), as substituted by No 25 2008. Original provision for disqualification of individuals was SISA s 120A(1), inserted by *Financial Sector Legislation Amendment Act (No 1) 2000*, No 160 2000. *Preuss v APRA* 05 ESL 08 [2005] AATA 784, decision affirmed with enforceable undertaking deemed not appropriate.

²⁵⁶ SISA s 126A(3), as substituted by No 25 2008. Original provision for disqualification of individuals was SISA s 120A(3), inserted by *Financial Sector Legislation Amendment Act (No 1) 2000*, No 160 2000. *Auton v APRA* 05 ELS 01 [2005] AATA 32, decision under review set aside; *VBN v APRA* 06 ESL 07 (i) decisions set aside because there was no contravention of SISA s 120A(2), (ii) decisions that two directors were not ‘fit and proper’ persons were set aside by AAT; *Re VCA v APRA* 08 ESL 04 [2008] AATA 580, decisions under review set aside.

²⁵⁷ SISA s 126A(5), as substituted by No 25 2008. Original provision for disqualification of individuals was SISA s 120A(5), inserted by *Financial Sector Legislation Amendment Act (No 1) 2000*, No 160 2000; SISA s 344.

²⁵⁸ SISA ss 126(6), (7); 344(6), (7).

²⁵⁹ SISA s 126H, as inserted by *Financial Sector Legislation Amendment (Review of Prudential Decisions) Act 2008*, No 25 2008.

²⁶⁰ SISA s 126K.

similar to those applicable to the disqualification by the Regulator.²⁶¹

7.5.1.2 *Auditors and actuaries*

The Regulator may make a written order (a ‘disqualification order’) disqualifying a person from being an approved auditor or actuary in certain circumstances.²⁶² The disqualification may be revoked on similar grounds and conditions that apply to the revocation of the disqualification of trustees.²⁶³

The Regulator may give written direction to the trustee of a superannuation entity to end the appointment of an auditor or actuary.²⁶⁴ The Regulator may apply to the Federal Court of Australia to have a person disqualified from being or acting as a person eligible to audit a superannuation entity.²⁶⁵

7.5.1.3 *Reporting and disclosure*

ASIC has powers under the CA to enforce and penalise for non-compliance with the provisions of that Act.

7.5.1.3.1 Reporting

If a director of a corporate trustee fails to ‘take all reasonable steps’ to comply with the financial records²⁶⁶ and reporting²⁶⁷ requirements of CA, ASIC may enforce the financial reporting

²⁶¹ SISA ss 126H(3)-(5).

²⁶² SISA s 131(1)-(4). 06 ESL 11, the AAT confirmed the decision of APRA to disqualify the applicant as an auditor under SISA s 131(1)), period of disqualification was for two years.

²⁶³ SISA s 131(4A)-(10).

²⁶⁴ SISA s 131AA, as inserted by *Financial Sector Legislation Amendment (Simplifying Regulation and Review) Act 2007*, No 154 2007.

²⁶⁵ SISA pt 16 div 3, as inserted by *Financial Sector Legislation Amendment (Review of Prudential Decisions) Act 2008*, No 25 2008.

²⁶⁶ CA pt 2M.2.

²⁶⁷ CA pt 2M.3.

provisions against the director on the civil standard of proof.²⁶⁸

Whilst the ultimate responsibility of the superannuation entity's compliance with the financial reporting laws is that of a director or an officer of the corporate trustee, if they conform with those provisions, they may still be liable in their capacity as an officer.²⁶⁹

7.5.1.3.2 Disclosure

The CA provides for enforcement of the provisions relating to financial product disclosure.²⁷⁰ These are by way of both criminal and civil liability.

The Criminal Code applies to all offences relating to financial product 'disclosure document or statement'.²⁷¹ A disclosure document or statement is 'defective' if it contains a misleading or deceptive statement, 'being a statement, or an omission, that would be materially adverse from the point of view of a reasonable person considering whether to proceed to acquire the financial product concerned'.²⁷²

The CA enables persons who have suffered loss or damage by reason of contraventions of the disclosure provisions to take civil action to recover their loss or damage.²⁷³

²⁶⁸ CA pt 2M.7; s 1317E.

²⁶⁹ CA pts 2M.2, 2M.3.

²⁷⁰ CA pt 7.9 div 7 subdivs A, B.

²⁷¹ CA ss 1021C-1021P. CA s 1021B (definition of 'disclosure document or statement' means:

- (a) a Product Disclosure Statement; or
- (b) a Supplementary Product Disclosure Statement; or
- (c) information required by paragraph 1012G(3)(a).

CA s 1012G(3)(a) relates to information required to be given to the client.

²⁷² CA s 1021B defines 'defective'.

²⁷³ CA s 1022B.

7.5.1.4 Stop orders

ASIC has the power to issue a stop order²⁷⁴ which effectively prevents any offer, issue, sale or transfer of securities taking place where it is satisfied that a breach of the provisions relating to the issuing of a disclosure document and that:

- (a) information in a disclosure document lodged with ASIC is not worded and presented in a clear, concise and effective manner;²⁷⁵
- (b) an offer of securities under a disclosure document lodged with ASIC contains misleading or deceptive statements and omissions;²⁷⁶
- (c) an advertisement or publication of a disclosure document is not in accordance with the restrictions on advertising and publicity.²⁷⁷

The trustee of a superannuation entity may seek a review of ASIC's decision to issue a stop order in the AAT²⁷⁸ or the Federal Court.²⁷⁹

7.5.1.5 Investigations by the Regulator

A Regulator can undertake an investigation of the affairs of a superannuation entity in prescribed circumstances.²⁸⁰ These circumstances would be those considered to affect the members' benefits.²⁸¹ The Regulator must inform the trustees by written notice²⁸² of an impending investigation of the whole or part of the

²⁷⁴ CA pt 6D.4. *Australian Securities and Investments Commission v Manito Pty Ltd* [2005] FCA 386; the orders against Shaun Oliver White and the PFS Group, ASIC M&IR 05-220 'ASIC shuts down self managed superannuation adviser', 1 August 2005.

²⁷⁵ CA s 715A.

²⁷⁶ CA s 728.

²⁷⁷ CA s 734.

²⁷⁸ CA pt 9.4A.

²⁷⁹ *Administrative Appeals Tribunal Act 1975*. In certain circumstances, *Administrative Decisions (Judicial Review) Act* s 5.

²⁸⁰ SISA pt 25 div 4.

²⁸¹ SISA s 264(1).

²⁸² SISA s 263.

affairs of the entity. Once this notice is issued, the Regulator may exercise a wide range of power to protect the members' benefits.²⁸³

These include:

- freezing assets;²⁸⁴
- entering premises and conducting inspections;²⁸⁵
- requiring production of documentation;²⁸⁶
- requiring assistance from and examining relevant persons;²⁸⁷
- requiring location of books and documentation and seizing them if not produced;²⁸⁸
- requiring identification of property of a superannuation entity.²⁸⁹

Whilst the *SISA*, the *ITAA* and the *CA* provide the Regulators with the power to regulate to protect members' benefits, make trustees accountable and minimise abuse, the Regulators are themselves dependent on the resources provided by the Federal Government. These resources are not only financial, allowing the Regulator to prosecute where deemed appropriate, but also skilled personnel with the ability to interpret and capacity and will to enforce the legislation. This ability to interpret the legislation should not be restricted to the *SISA* and the *CA* but also implementation of other Acts in the various jurisdictions.²⁹⁰

²⁸³ *SISA* s 264.

²⁸⁴ *SISA* ss 264(3), (3A), (4), 264(4A).

²⁸⁵ *SISA* ss 265-268.

²⁸⁶ *SISA* s 269.

²⁸⁷ *SISA* s 270.

²⁸⁸ *SISA* ss 271-274.

²⁸⁹ *SISA* s 275.

²⁹⁰ *Kernahan v ACN 003 134 475 Pty Ltd (formally known as LifeTrack Management Ltd)* [2010] NSWSC 51: an investigative report commissioned by APRA was not admissible under *SISA* s 295 as prima facie evidence in civil proceedings due to an invalid delegation by an Inspector.

Gardener and APRA [2009] AATA 990: AAT set aside disqualification of director of HIH as not being a 'fit and proper' person on the interpretation of this term.

7.5.1.6 Court protection

If the Regulator considers it necessary to protect the members' benefits, it may apply to the Court to make an order to protect those benefits. This may be, inter alia, the appointment of a receiver or receiver and manager of property, prohibition on sending money out of Australia or prohibiting a person from leaving Australia.²⁹¹

7.5.2 Commissioner of Taxation

The Commissioner of Taxation uses the powers provided to deter tax avoidance.

7.5.2.1 Part IVA

The general anti-avoidance provisions may be applied to arrangements involving superannuation funds.²⁹² The *Crimes (Taxation Offences) Act 1980* creates a number of criminal offences relating to the fraudulent evasion of various federal taxes, including income tax and superannuation. A person convicted of an offence may also be ordered to pay some, or all, of the tax involved.²⁹³

7.5.2.2 Tax avoidance schemes

The *Tax Administration Act 1953* ('TAA') provides a deterrent against:

- the promotion of tax avoidance schemes and tax evasion schemes; and
- the implementation of schemes that have been promoted on the basis of conformity with a product ruling in a way that is

²⁹¹ SISA s 313(1A), inserted by *Superannuation Industry (Supervision) Legislation Amendment Act 1995*, No 144 1995.

²⁹² *Taxpayer Alerts* TA 2003/1, TA 2008/3; *ITAA* pt IVA ss 177A-H, as inserted by No 110 1981; s 260 (not applicable after 27 May 1981).

²⁹³ *Crimes (Taxation Offences) Act 1980* s 12.

materially different from that described in the product ruling.²⁹⁴

An entity is a promoter of a tax exploitation scheme if:

- the entity markets the scheme or otherwise encourages the growth of the scheme or interest in it;
- the entity or an ‘associate’ of the entity receives (directly or indirectly) consideration in respect of that marketing or encouragement, and
- having regard to all relevant matters, it is reasonable to conclude that the entity has had a substantial role in respect of that marketing or encouragement.²⁹⁵

An employee is not to be taken to have had a substantial role in respect of the marketing or encouragement merely because the employee distributes information or material prepared by another entity.²⁹⁶ An entity is not a promoter merely because the entity provides advice about the scheme.²⁹⁷

The Commissioner may:

- request the Federal Court to impose a civil penalty;²⁹⁸
- seek an injunction to stop either the promotion or implementation of a tax exploitation scheme does not conform to its product ruling;²⁹⁹
- enter into voluntary undertakings with promoters or implementers that address concerns about the way in which the schemes are being promoted or implemented.³⁰⁰

²⁹⁴ TAA Sch 1 Pt 4-25.

²⁹⁵ TAA Sch 1 s 290-60(1).

²⁹⁶ TAA Sch 1 s 290-60(3).

²⁹⁷ TAA Sch 1 s 290-60(2).

²⁹⁸ TAA Sch 1 sub-div 290-B.

²⁹⁹ TAA Sch 1 sub-div 290-C.

³⁰⁰ TAA Sch 1 sub-div 290-D.

The Federal Court may impose a maximum penalty which is the greater of:

- 5,000 penalty units for an individual or 25,000 penalty units for a body corporate; and
- twice the consideration received or receivable, directly or indirectly, by the entity or its associates in respect of the scheme.³⁰¹

Defences to the application of penalties are available.³⁰²

7.6 Related legislation

Legislation was enacted to provide a mechanism for members to complain about the conduct of a trustee. Legislation was also enacted to provide employees with the right to choose the fund they wish to participate in.

7.6.1 Resolution of Complaints

The Superannuation Complaints Tribunal was established on 1 July 1994 by the *Superannuation (Resolution of Complaints) Act 1993*, ('SRCA').³⁰³ The Tribunal was available to all superannuation funds and approved deposit funds, except 'excluded funds'³⁰⁴, regulated by the ISC under the *SISA*. The *SRCA* is currently available to members.

The procedures for both the complainants and the Tribunal are detailed in the *SRCA*. The Tribunal will not deal with any complaint

³⁰¹ TAA Sch 1 s 290-50.

³⁰² TAA Sch 1 s 290-55.

³⁰³ *Superannuation (Resolution of Complaints) Act 1993*, No 80 1993. Senate Select Committee, *Super Complaints Tribunal* (December 1993); Senate Select Committee, *Review of Superannuation Complaints Committee* (April 1996).

³⁰⁴ *SISA* s 10(1), (definition of an 'excluded fund' meant:

- an excluded superannuation fund, ie a fund with fewer than five members;
- an excluded approved deposit fund ie a fund with only beneficiary and, if established on or after 1 July 1994, where the eligible termination payments of the beneficiary invested with the fund had an initial value of at least \$400,000).

about a trustee's decision unless an attempt has been made to resolve the complaint by an internal dispute arrangement. Reasonable attempts to resolve other complaints have to be undertaken prior to making a request for the Tribunal to become involved.³⁰⁵ If unsuccessful, the Tribunal has to attempt to resolve a complaint by conciliation through conferences with the parties involved.³⁰⁶ If this process fails, the Tribunal has to review the decision of the trustee to which the complaint relates. Under the review process, a reference to the Federal Court may be made against a Tribunal decision on a question of law.³⁰⁷ In its review, the Tribunal has all the powers, obligations and discretions conferred on the trustee by law or under the governing rules of the fund.³⁰⁸ The Tribunal's determination has to be notified to all relevant parties. The Tribunal is required to report any contravention of any law of the governing rules to the ISC.³⁰⁹

An appeal to the Federal Court of Australia against the determination may be made by the complainant.³¹⁰

7.6.2 Choice of fund

The choice of fund rules applied from 1 July 2005.³¹¹ Under the choice of fund, employers must allow eligible employees³¹² to choose an eligible fund³¹³ into which their Superannuation

³⁰⁵ SRCA s 19; Superannuation Circular No I.E.I., dated December 1994.

³⁰⁶ SRCA Pt 5.

³⁰⁷ SRCA pt 7.

³⁰⁸ SRCA pt 6.

³⁰⁹ SRCA s 64.

³¹⁰ SRCA pt 7.

³¹¹ *Superannuation Guarantee (Administration) Act 1992* ('SGAA'), pt 3A (ss 32A-ZAA), as inserted by *Superannuation Legislation Amendment (Choice of Superannuation Funds) Act 2004*, No 102 2004.

³¹² SGAA pt 3A div 2.

³¹³ SGAA pt 3A div 3.

Guarantee ('SG') contributions are to be paid. Penalties in the form of an increased SG charge may be imposed for non-compliance.³¹⁴

The Federal Government made provisions for eligible employees to make their own decision on where they wished to save for their retirement. Together with the disclosure requirements of trustees, including fees and performance, employees could make an informed decision and plan for their retirement.

7.7 Bankruptcy Act

The definition of 'divisible property' in the *Australian Bankruptcy Act 1966* ('*Bankruptcy Act*') provides:

Subject to this Act:

- (a) all property that belonged to, or was vested in, a bankrupt at the commencement of the bankruptcy, or has been acquired or is acquired by him or her, or has devolved or devolves on him or her, after the commencement of the bankruptcy and before his or her discharge; and ...³¹⁵

The initially inserted exception to the definition of divisible property protected a member's benefits:

...

- (d)(iii) the interest of the bankrupt in:
 - (A) a regulated superannuation fund (within the meaning of the *Superannuation Industry (Supervision) Act 1993*); or
 - (B) an approved deposit fund (within the meaning of that Act); or
 - (C) an exempt public sector superannuation scheme (within the meaning of that Act);³¹⁶

Where a member becomes absolutely entitled to a benefit, ie it is the property of the member, the benefit becomes vested in the official trustee in bankruptcy in the event of bankruptcy. In the

³¹⁴ SGAA ss 19(2A)-(2B), 19(A); pt 6-8.

³¹⁵ Ibid s 116(1).

³¹⁶ *Australian Bankruptcy Act 1966*, s 116(2), as inserted by No 12 1980.

absence of entitlement to the benefits, trustees of superannuation funds are to exercise their powers for the purposes of benefiting members, not the creditors in the bankrupt estate of one of the beneficiaries.³¹⁷

Prior to 1 July 1994, a ‘forfeiture’ provision in a superannuation trust deed purporting to disentitle the member to benefit in the event of bankruptcy made access to superannuation benefits impossible unless the deed or some of its clauses could be set aside. In the *Bond Case*, Hill J made the obiter remark that ‘a properly worded forfeiture clause will continue to defeat a trustee in bankruptcy’.³¹⁸

After 1 July 1994, a number of amendments were made to the *Bankruptcy Act*, commencing 1 July 1994.³¹⁹ Section 302A was introduced to prevent the use of a valid forfeiture clause to defeat the purpose of the *Bankruptcy Act*.³²⁰

Official trustees in bankruptcy used s 121 of the *Bankruptcy Act*, the provision to void transactions which were implemented to defeat creditors, to recover money paid into a superannuation fund with mixed success.³²¹

³¹⁷ *Dwyer v Ross* (1992) 34 FCR 463, quoting *R v Williams, the Law and Practice in Bankruptcy* (15th ed). 237, *G Farwell, Powers* (3rd ed 1916), Ch X, *Duke of Portland v Topham* (1864) 11 HLC 32, 54, *Vatcher v Paull* [1915] AC 372, 378.

³¹⁸ *Re Bond: Ex parte Ramsay* (1992) 25 ATR 61; upheld on appeal in *Caboche v Ramsay* (1993-4) 119 ALR 215.

³¹⁹ *Superannuation Industry (Supervision) Consequential Amendments Act 1993*, No 82 1993.

³²⁰ *Australian Bankruptcy Act 1966* s 116(2)(d)(iii), as inserted by *Superannuation Industry (Supervision) Consequential Amendments Act 1993*, No 83 1993.

³²¹ In *Official Trustee in Bankruptcy v Trevor Newton Small Superannuation Fund Pty Ltd* (2001) 114 FCR 160, the trustee in bankruptcy successfully argued that the main purpose in making the transfer to the superannuation fund was to defeat the creditors. In *Benson v Cook* (2003) 214 CLR 370, the appeal to the High Court by the trustee in bankruptcy was dismissed by majority. The issue was whether the recipient corporate superannuation trustees could be described as ‘purchasers’ for ‘valuable consideration’. The payments were made at the direction of the debtor, out of funds due to the debtor

Subsequent to the High Court decision in *Benson v Cook*,³²² an amendment to the exception to the definition of divisible property was made to the *Bankruptcy Act*³²³ to allow bankruptcy trustees to recover superannuation contributions made prior to bankruptcy with the intention to defeat creditors. The exceptions were included in section 128B,³²⁴ 128C³²⁵ and 139ZU.³²⁶

Whilst members' benefits are protected within the superannuation entity, an annuity or pension from a superannuation fund is treated as income for the purposes of the income contribution provisions.³²⁷

Protection of accumulated members' benefits within superannuation funds in the event of a member's bankruptcy is in line with the Federal Government's policy to encourage people to save for their own retirement. The protection provides confidence for contributors that savings within superannuation funds cannot be claimed by a trustee in bankruptcy except where the contributions have been made or transactions entered into for the purpose of defeating creditors. The amendments made to the *Bankruptcy Act* have clarified the treatment of superannuation benefits in bankruptcy.

under an existing superannuation scheme, by way of contributions to other, commercially marketed, superannuation schemes for rights and benefits to which the debtor would in due course become entitled under the rules of each scheme. Those rights and benefits constitute substantial and valuable consideration for the contributions of the debtor.

³²² See above n 321.

³²³ Inserted by *Bankruptcy Legislation Amendment (Superannuation Contributions) Act*, No 57 2007, effective 28 July 2006.

³²⁴ Superannuation contributions made to defeat creditors – contributor is a person who later becomes a bankrupt.

³²⁵ Superannuation contributions made to defeat creditors – contributor is a third party.

³²⁶ Order relating to rolled-over superannuation interests.

³²⁷ *Australian Bankruptcy Act 1966*, pt VI div 4B, sub-div C s 139L.

7.8 Conclusion

By designing the *SISA* to rely on the taxation power, corporations power and the pension power, the Federal Government was able to provide wider powers for the Regulators to regulate superannuation entities. These powers included effective enforcement of prudential requirements and obligations imposed on trustees. The combination of the Regulators³²⁸ with the prescriptive legislation³²⁹ provides protection for members' benefits and makes the trustees accountable for their actions. The audit process minimises the possibility of fraud and theft. The members' benefits are potentially well protected.

An integral part of success of the superannuation industry is dependent on the role of the trustees and their compliance with the operational duties required by the *SISA*. The operational duties have evolved to a comprehensive list that is designed to protect members' benefits. The *SISA* has endorsed this role and has provided the Regulator with the power to enforce it. It has, in turn, provided trustees the right to have decisions made by the Regulator reviewed.

The Federal Government has again appointed committees to advise it on the implementation of its retirement income policy. The staged implementation has provided a stable introduction to each phase. Firstly, there was the enactment of the *SISA*, followed by the introduction of the associated regulations. Secondly, APRA was established for the prudential supervision, not only of superannuation entities but also banks and insurance companies. Then there was the renaming of 'excluded superannuation funds' to 'self managed superannuation funds' and their relocation to the

³²⁸ APRA, ASIC and ATO.

³²⁹ *SISA*, *CA*, *TAA* and *ITAA* 97 (initially *ITAA*).

ATO for their regulation of non-prudential matters. Finally and perhaps most significant in the evolution of the regulation of superannuation entities was the introduction of the licensing and registration provisions. As a consequence to the introduction of these provisions, APRA developed a prudential review system and ASIC supervised the disclosure and reporting of the RSEs.

The system of penalties and sanctions provided by both the *SISA* and *CA* are shown to be substantial and should be a deterrent against non-compliance with these Acts.

The introduction of the *SISA* with the operational, licensing and penalty provisions and APRA have provided the framework that the Federal Government needs to protect members' benefits and make trustees accountable for their responsibilities. The framework also includes provisions to discourage and minimise, if not prevent, the abuse of the superannuation system.

CHAPTER 8

CONCLUSION

The hypothesis of this thesis is:

The evolution of the legislation regulating superannuation funds has been consistent with the Federal Government's policy intent to encourage people to save for their own retirement. The Federal Government has implemented its policy by amending the legislation regulating superannuation funds to protect the members' benefits for their retirement and to ensure the members' entitlements are available when required. It has made trustees of superannuation funds accountable for their responsibilities and included provisions within the legislation to prevent abuse of the superannuation system.

A priority of the Federal Government is to raise sufficient revenue to cover expenditure with an equitable and efficient allocation of the tax burden. Part of this expenditure is payment of pensions to the aged.

The basis for the retirement policy arose because the analysis of the demographics and economic projections indicated that the social security system could not support retirees indefinitely. The Federal Government had to take a proactive role in planning and developing strategies for providing retirement income for the population.

The hypothesis of this thesis is whether the evolution of the legislation regulating superannuation funds has been consistent with the Federal Government's policy intent to encourage people to save for their own retirement. The analysis shows that the Federal Government's policy intent to encourage people to save for their retirement has not changed. It shows that the legislation regulating superannuation funds has evolved to protect members' benefits for their retirement, to ensure that the members' entitlements are

available when required, to make the trustees accountable for their responsibilities and to minimise abuse of the superannuation system. The regulation as it has evolved provides a system which people should be able to rely on as a credible vehicle to save for their retirement. The evolution of the legislation regulating superannuation funds has been consistent with the Federal Government's policy intent to encourage people to save for their own retirement. This is evident by the current legislative framework.

The current regulation

The legislative framework that regulates the superannuation entities provides the structure, a statutory trust, in which the trustee acts in that capacity to protect members' benefits. For the successful operations of a superannuation fund, a trustee must be a 'fit and proper' person.

The Federal Government adopted a structure for superannuation funds with less than five members, 'self managed superannuation funds', in which the conditions include, inter alia, that the members must be trustees and the trustees must be members. It was asserted that Trustees would be able to protect their own interests and these funds were subjected to a less onerous prudential regime under *SISA*.

For all other funds, a Regulator, the Australian Prudential Regulation Authority ('APRA'), controls the appointment of the trustee under the licensing provisions in the *Superannuation Industry (Supervision) Act 1993* ('SISA'). The *SISA* provides for the registration of registrable superannuation entities ('RSE'). Only a licensed trustee, a RSE licensee, may apply to APRA for the registration of an RSE. This application requires, inter alia, the provision to APRA of the proposed risk management plan. This

process provides a mechanism for the establishment of a superannuation entity.

The duties and obligations of the trustee are specified in the *SISA*. The ongoing operation of a superannuation entity involves the trustee performing these duties and obligations. They protect members' benefits. The trustee must also comply with the reporting and disclosure requirements of the *Corporations and Securities Legislation ('CA')*. The trustee is required to provide disclosure documents to a prospective member and ongoing reports to members. This function ensures that members are fully informed about their savings and the performance of the superannuation entity that holds their savings.

APRA reviews the ongoing operations of the superannuation entity, including the trustee's compliance with the provisions of the *SISA* and the terms and conditions of the licence. It also reviews the adherence by the trustee to the risk management plan for, and the performance of, the superannuation entity.

Another Regulator, Australian Securities and Investment Commission ('ASIC'), controls information provided to potential and current members of a superannuation entity.

The requirements for the trustee of a superannuation fund to appoint an approved auditor and for there to be an audit carried out every year, have actuarial investigations carried out, when appropriate, and to report annually to the APRA on the performance of the superannuation entity provide an additional assurance as to the veracity of the superannuation entity and integrity and competency of the trustee.

The Regulators make trustees accountable for the responsibilities of protecting members' benefits. In addition to reviewing the

standards of operating by and the reporting of the trustees, the SISA and the CA provide the mechanism to impose penalties, in most instances connected with the *Criminal Code Act 1995*, for non-compliance. APRA also has the power to disqualify or remove trustees, auditors and actuaries. The Australian Taxation Office ('ATO') can apply anti-avoidance provisions of the *Income Tax Assessment Act 1936* ('ITAA') and the *Crimes (Taxation Offences) Act 1980*. Criminal offences relating to the fraudulent evasion of taxes can result in a person convicted of an offence being ordered to pay some, or all, of the tax involved and other penalties. ASIC can issue a stop order on disclosure documents if it considers that there is a breach of the provisions relating to issuing the disclosure document.

To protect members' benefits APRA may undertake an investigation of the affairs of a superannuation entity in prescribed circumstances that may result in action to, for example, freeze assets. APRA can also apply to the Federal Court to appoint a receiver or receiver and manager of property of the superannuation entity if it considers the members' benefits are at risk.

Members have the right to be fully informed about the activities of a superannuation entity and to complain about a trustee's decision. They are informed about their benefits and the fees and costs allocated to their member's account. They can also claim damages from the trustee for negligence or fraudulent behaviour. In certain circumstances, members can choose the superannuation fund for their contributions.

The evolution

This framework has evolved since the enactment of the ITAA. It has been a gradual process with staged implementation. The Federal Government has sought advice, considered it and taken those

recommendations to support its policy. There has been a bi-partisan approach to the implementation of superannuation policy. The evolution can be seen to be three phases, all connected with circumstances that required the Federal Government's attention. Firstly, there were the measures to encourage people to save for their retirement. Secondly, there was the protection of members' benefits. This occurred with the introduction of the *Occupational Superannuation Standards Act* ('OSSA') that replaced the regulation by the *ITAA*. Thirdly, there was making trustees accountable for their responsibilities. This occurred with the introduction of the *SISA*, which replaced the *OSSA*.

There were a number of components relating to the retirement income policy that influenced the evolution of superannuation funds. These were:

- the Federal Government's strategy;
- the trust structure;
- the taxing provisions;
- the regulation of superannuation funds;
- the regulators.

Federal Government's strategy

Initially, providing retirement income depended on voluntary contributions to superannuation funds and government provided pensions. The voluntary contributions attracted tax incentives provided there was compliance with the provisions of the *ITAA*. In acknowledgement of the ageing population and the increase in those in receipt of the aged pension, the Federal Government, in collaboration with unions and employers, provided a strategy for compulsory contributions by employers for their employees. These compulsory contributions also attracted tax incentives provided there was compliance with the provisions of the *ITAA*.

The trust structure

The vehicle to receive contributions for superannuation savings evolved from a trust structure to a 'statutory trust'. This provided the basic structure on which superannuation funds evolved. This change was achieved as was seen in Chapter 2 by defining what the trust represented. The regulation of trusts was transferred from the various States of Australia to the Federal Authority, APRA, established for the regulation of, inter alia, superannuation funds under specific regulatory legislation, the *SISA*.

Taxation

A tool readily available to any government to be applied as both an incentive and a deterrent is taxation. Taxation is a form of compulsory contribution from the private to the public sector to support intended government expenditure.¹ It is, as Holmes J in *Compania de Tabacos v Collector De Filipinas*² said, the price paid for a civilised society.

The Federal Government encouraged people to participate in superannuation funds by providing incentives in the form of tax concessions to superannuation funds, contributors and beneficiaries. As was discussed in Chapter 3, these tax incentives initially were provided for superannuation funds established for the benefit of employees only. The Federal Government recognised the inequity of this situation and the need to encourage all members of society to save for their retirement. A number of different types of superannuation funds developed within the *ITAA* that provided concessional tax treatment. This tax treatment also had inequities with different superannuation funds attracting different concessions. Eventually, under the *ITAA*, the income of superannuation funds established to provide benefits for members

¹ Jeffrey Waincymer J *Australian Income Tax Principles and Policy*, (Butterworths, 2nd ed, 1993) 2.

² 275 US 87 (1927).

for retirement purposes was exempt from income tax provided they complied with the provisions of this Act.

In 1988, with the potential introduction of compulsory contributions in the near future, the increase in voluntary contribution and the ageing population, the Federal Government considered the cost of the retirement income policy needed to be addressed. To enable the Federal Government to continue to provide tax incentives to support its retirement income policy, a concessional rate of income tax was introduced.

Providing these tax incentives was seen to be successful. There was increasing participation in saving for retirement. With tax incentives, in 1974, 32% of the total workforce covered by superannuation increased from 32% in 1974 to 39% by 1983, and 72% by 1992. The tax incentives combined with the compulsory superannuation contributions resulted in an increase to 80.5% by 1995 and 90% by 2006.

Regulation of superannuation entities

From 1936, different types of superannuation funds evolved in an attempt to encourage different categories of people to save for their retirement. The Federal Government's efforts to implement their policy to encourage people to save for their own retirement has resulted in superannuation being potentially available to all.

During the 1970s and early 1980s, tax avoidance was rampant. This was of concern to the Federal Government because it affected the Revenue by reducing the amount of tax collected and members' benefits were not secure. As is seen in Chapters 4 and 5, there were inequities and abuse of the superannuation system. Chapter 6 analysed the Reports by various Committees appointed by the Federal Government. There was a common theme in all Reports. Members' benefits were not secure. The recommendations were for

vesting and preservation of these benefits together with their portability. This would lay the foundation of the protection of members' benefits and encourage saving by using the superannuation system.

Then followed in 1987, the introduction of the OSA with its associated regulations ('OSR') and the establishment of a new regulatory body, the Insurance and Superannuation Commission ('ISC'). This new regulatory framework protected members' benefits. It allowed members to identify their benefits, take ownership of them and secure them for their retirement.

Whilst the introduction of the OSA provided protection for members' benefits as was described in Chapter 6, the trustees were not accountable for their responsibilities. In Chapter 7, it was shown that the trustee of a superannuation fund had evolved into a pivotal role in the operations of a superannuation entity. The ISA was introduced in 1993 to remedy the problem associated with the operations of superannuation funds by trustees.

The ISA evolved to include other complementary legislation that currently regulates superannuation funds. It regulates the quality and competency of trustees appointed to operate the superannuation entities and the disclosure of information making members fully informed about their retirement savings. It imposes penalties and makes the trustees accountable for their responsibilities.

There are a number of acts involved in the regulation and implementation. Whilst making the system complex, it provides for a framework that instils confidence in the people, encourages saving for retirement by providing tax incentives and protects members' benefits by making trustees responsible for this protection and accountable.

The Regulators

The supervision of the regulation progressed from the ATO, to the Insurance and Securities Commission, to ATO, APRA and ASIC. The evolution took into account the perceived need at the time of their establishment and the consideration of the application of the *Constitution*. The development of the combination of ATO, APRA and ASIC was to enable these authorities to perform their duties efficiently, reduce duplication of their functions and protect members' benefits. The ATO regulates self managed superannuation funds and continues in its tax assessment role of superannuation entities. APRA has the prudential role of regulating superannuation entities including the licensing of trustees and registering RSEs. ASIC protects the members by regulating the issue of disclosure statements and the reporting activities of the trustees.

The evolved regulation of the superannuation industry provides a system that allows trustees to operate the superannuation entities and members to plan their retirement. The Regulators have the powers to enforce compliance with the legislative regulations.

Whilst there may be a need for minor amendments to clarify the legislative regulations of superannuation entities, the Federal Government has implemented its policy intent. It has provided a legislative framework that encourages people to save for their own retirement by providing tax incentives, protects the members' benefits so that the benefits will be available when required and makes trustees accountable for their responsibilities. It provides mechanisms to minimise, and penalties to deter, abuse. It is now up to the people to take the responsibility to assist the Federal Government in its endeavours to provide for their own retirement. The decision for investing their retirement savings must be made by the members. Seeking advice, if it is required, from licensed

investment advisers is their responsibility. The information provided to them should give them and their advisers adequate information to assess the finance product. In the absence of fraud or negligence by the trustee, for which, under the *SISA*, a member can claim damages, the Federal Government has provided a regulated environment for the market forces to work in. The Federal Government is dependent on the efficiency of the Authorities to make the regulation effective. It must, however, provide sufficient resources, both human and financial, to allow the Authorities to enforce the regulations. The quality and skills of the personnel is a major factor in the success of the regulation of superannuation entities. The skills required by the personnel of the Regulators must be comparable with, if not better than, the skills of trustees and those engaged to advise them. The Federal Government is also dependent on the goodwill of the people and their advisers. The Federal Government cannot, nor should it attempt to, legislate against greed or ignorance.

Future research could include the recently released reports, the Henry Report³ and the Cooper Review.⁴ The methodology and structure adopted in this current thesis could be applied to the evolution of the legislation regulating superannuation funds once the Federal Government has considered and decided which recommendations of the Henry Report and the Cooper Review should be implemented.

The effectiveness of the regulation of self managed superannuation funds could be analysed in light of the significant increase in the number of these types of funds and the amount of assets accumulated within them. The qualifications and knowledge of the trustees must be of concern to the Federal Government when

³ Taxation Review Panel, *Australia's Future Tax System Report to the Treasurer* (2009).

⁴ Superannuation Review Panel, *Review of the Governance, Efficiency, Structure and operation of Australia's Superannuation System* (2010).

considering the complexities of the legislation and regulations and the possible abuse, deliberate or not, resulting in leakage of the Revenue.

The effectiveness of the supervision of the regulation of superannuation funds by the ATO, APRA and ASIC, whilst audited by the Auditor General, could be reviewed by an independent review committee. This review could assess the quality and qualifications of staff involved in the supervision process. The quantity of appropriate staff for effective supervision could be the basis of this review. Success of prosecutions taken by these Authorities could also be reviewed.

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ISC Circular No 18	Relocation of former provisions of Income Tax Assessment Act as operating standards, status of income tax ruling, approved ancillary purposes, October 1990
ISC Circular No 24	Superannuation supervisory levy, late lodgment fees, operating standards amendments, September 1991
ISC Circular No 28	Operating standards: Reporting to members, July 1992
ISC Circular No 32	Prospectus requirements for publicly offered superannuation funds, February 1993
ISC Circular No 33	Superannuation guarantee arrangements, May 1993
ISC Circular No 37	Prospectus requirements for publicly offered superannuation funds, August 1993

APRA Superannuation Guidance Notes

SGN 110.1	Fit and Proper
SGN 120.1	Risk Management
SGN 130.1	Outsourcing
SGN 140.1	Adequacy of Resources
SGN 150.1	Capital Requirement – Net Tangible Assets

REFERENCES

ASIC Regulatory Guidelines and Policy Statements

Policy Statement 181 Licensing: Managing Conflict of Interest

RG 168 Product statements (and other disclosure obligations) including Good Disclosure Principles